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IN THE

# Supreme Court of the United States

BENEDICTO V. YUJUICO, TERESITA M. YUJUICO AND THE BVY GROUP, INC.,
PETITIONERS,

*VS.*

FIRST PACIFIC BANK LIMITED, A HONG KONG BANKING CORPORATION,
RESPONDENT.

**ON PETITION FOR WRIT OF CERTIORARI TO THE CALIFORNIA COURT OF APPEAL FOR THE FIRST APPELLATE DISTRICT**

## PETITION FOR WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

1. Whether California law permitting a court to unilaterally determine that an arbitration dispute is "wholly groundless", and thereby refuse to enforce a contractual arbitration agreement governed by the Federal Arbitration Act pursuant to which the parties have expressly agreed to submit all disputes regarding arbitrability to an arbitrator, unlawfully preempts the Federal Arbitration Act in violation of the Supremacy Clause of the United States Constitution.

2. Whether an ex parte judgment of foreclosure and order of sale of a private residence entered without the parties' bargained for notice violates the due process clause of the Fourteenth Amendment of the Federal Constitution.

## PARTIES TO THE PROCEEDINGS

All parties to the proceedings below are listed in the caption. Petitioner The BVY Group, Inc., is a California corporation wholly owned by Petitioners Benedicto and Teresita Yujuico, husband and wife. There are no parent corporations nor any publicly held companies which hold any stock in Petitioner The BVY Group, Inc.

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IN THE

# Supreme Court of the United States

## PETITION FOR WRIT OF CERTIORARI

Petitioners Benedicto V. Yujuico, Teresita M. Yujuico and the BVY Group, Inc., respectfully pray that a Writ of Certiorari issue to review the judgment below.

### *I. OPINIONS BELOW*

The decision of the California Court of Appeal is unreported; it is reprinted in the Appendix to this Petition at p. A-1. The Judgment of the Superior Court for the County of San Mateo is reprinted in the Appendix at p. B-1. The decision of the California Supreme Court denying review is reprinted in the Appendix to this Petition at p. C-1.

### *II. JURISDICTIONAL STATEMENT*

On July 24, 2000, the California Supreme Court filed its decision denying review of the California Court of Appeal's decision entered on June 15, 2000. Pursuant to 28 U.S.C. § 1257, this Court has jurisdiction to review on a writ of certiorari the decision of the California Court of Appeal.

### *III. CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED*

Article VI, Section 2 of the Constitution of the United States states as follows:

> "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and

the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding."

Section 1 of the Fourteenth Amendment to the Constitution provides in pertinent part:

". . . No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

9 USC § 2, states as follows:

"A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon any such grounds as exist at law or in equity for the revocation of any contract."

## *IV. STATEMENT OF THE CASE*

This action was instituted by Respondent's ex parte application for entry of a judgment of foreclosure and order of sale ("Judgment") of Petitioners' family residence in Atherton, California ("Residence"), claiming that Petitioners had defaulted on a loan payment.

Petitioners opposed the ex parte application on the ground that the parties had a written agreement ("Agreement") to arbitrate all disputes governed by the Federal Arbitration Act, 9 U.S.C. §§ 1, et seq. ("FAA"), that Petitioners had properly demanded arbitration, and that Respondent could not apply directly to the courts for entry of the Judgment under the terms of the Agreement.

The parties' arbitration clause states, at paragraph 19 of the Agreement:

> "In the event of any dispute relating to or arising out of this agreement, the exclusive forum for resolution of any such dispute shall be by arbitration in San Francisco under the authority of JAMS/ENDSIPUTE in accordance with the International Rules of the American Arbitration Association." (CT 151.)

Article 15.1 of the International Arbitration Rules of the American Arbitration Association ("AAA") states that *"the tribunal shall have the power to rule on its own jurisdiction, including any objections with respect to the existence, scope or validity of the arbitration agreement".*

Article 15.3 of the Rules further states that *"a party must object to the jurisdiction of the tribunal or to the* ***arbitrability of a claim*** *or counterclaim no later than the filing of a statement of defense as provided in Article 3 . . ."* [Emphasis added.]

Respondent refused to submit the dispute to arbitration, claiming it was a sham and that the arbitration clause did not require submitting disputes regarding arbitrability to the arbitrator.

On October 9, 1998, during an ex parte proceeding, the Superior Court granted Respondent's application and entered the Judgment. Respondent immediately sold the Residence to itself by credit bidding its own secured interest. Petitioners were recently evicted from the Residence on October 3, 2000.

On June 15, 2000, the California Court of Appeal for the First Appellate District affirmed the Judgment, basing its opinion on the California Supreme Court decision in *McCarroll v. L.A. County etc. Carpenters,* 49 Cal.2d 45, 315 P.2d 322 (1957) (*"McCarroll"*).

The *McCarroll* decision permits judicial consideration of the merits of a dispute governed by the FAA *before* submitting

the matter to arbitration if the superior court determines that the claim is "wholly groundless"; notwithstanding the express contractual intent of the parties to reserve jurisdiction exclusively to the arbitrator under Articles 15.1 and 15.3 of the International Arbitration Rules of the AAA.

Thus, the *McCarroll* decision creates an unlawful peremptory gatekeeping exception to enforcement of arbitration agreements governed by the FAA which may be unilaterally exercised by the court even when the parties have expressly agreed to submit all disputes regarding jurisdiction and the arbitrability of a claim to arbitration, thereby pre-empting the Federal Arbitration Act in violation of the Supremacy Clause of the United States Constitution.

The peremptory judicial gatekeeping exception created by the *McCarroll* decision is also in direct conflict with this Court's decisions in *First Options of Chicago v. Kaplan*, 514 U.S. 938, 944, 131 L.Ed.2d 985, 115 S.Ct. 1920 (1995) ("*First Options*"); *Allied-Bruce Terminix Companies, Inc. and Terminix International Company v. Dobson*, 513 U.S. 265, 130 L.Ed.2d 753, 115 S.Ct. 834 (1995) ("*Allied-Bruce*"); *Perry v. Thomas*, 482 U.S. 483, 96 L.Ed.2d 426, 107 S.Ct. 2520 (1987); *Southland Corp. v. Keating*, 465 U.S. 1, 79 L.Ed.2d 1, 104 S.Ct. 852 (1984) ("*Southland*") and *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24, 74 L. Ed. 2d 765, 103 S. Ct. 927 (1983).

Petitioners filed a Petition For Review of the Court of Appeal's opinion with the California Supreme Court on July 20, 2000, which was denied on July 24, 2000.[1] Petitioners obtained a 60-day stay of enforcement of the Judgment from the California Superior Court for the County of San Mateo, which stay expired on September 24, 2000.

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[1] Petitioners obtained such quick review of the Petition because they also requested an immediate stay of the Judgment in a companion Petition. That stay request was denied.

On September 14, 2000, Petitioners filed a complaint seeking rescission of the parties' Agreement with the United States District Court for the Northern District of California, based on their mistake as to the enforceability of their agreement to arbitrate all disputes in accordance with the International Arbitration Rules. On September 19, 2000, Petitioners filed an application for a temporary restraining order in the District Court, seeking a preliminary injunction restraining enforcement of the Judgment.

On September 22, 2000, the Honorable Phyllis J. Hamilton, United States District Court Judge, denied Petitioners' application, finding that the rescission action did not raise a federal claim, and that federal statutory authority over direct appeals from the state courts [including federal claims "inextricably interwined" with those a state court has already decided], lies exclusively with this Court pursuant to *Rooker v. Fidelity Trust Co.*, 263 U.S. 413, 68 L.Ed. 362, 44 S.Ct. 149 (1923), and *District of Columbia Court of Appeals v. Feldman*, 460 U.S. 462, 75 L.Ed.2d 206, 103 S.Ct. 1301 (1983). Pursuant thereto, Petitioners voluntarily dismissed the rescission action.

On September 28, 2000, Petitioners filed a petition for immediate stay of the Judgment pending certiorari by this Court with the Court of Appeal. That petition was denied on October 2, 2000. On October 3, 2000, Petitioners submitted an Application For Stay Of Mandate of the Opinion of the California Court of Appeal and the Judgment of the Superior Court of the State of California, County of San Mateo, to the Honorable Sandra Day O'Connor, Case No. 00-A286. Associate Justice O'Connor denied Petitioners' Application on October 4, 2000.

Review must be granted to resolve the conflict between the *McCarroll* decision and the enforceability of arbitration agreements governed by federal law, in order to preserve the integrity of the FAA and the Supremacy Clause of the United States Constitution. Otherwise, state courts will be free to pre-empt federal arbitration law.

The time is ripe for review of this issue. Indeed, the California Supreme Court recognized back in 1957 that the

*McCarroll* opinion was in "irreconcilable conflict" with some of the federal decisions at that time. (*McCarroll, supra*, 49 Cal.2d at 67.)

Further, the *McCarroll* decision has already been partially abrogated by this Court in *Drake Bakeries v. Bakery Workers* 370 U.S. 254, 8 L. Ed. 2d 474, 82 S. Ct. 1346 (1962), which held—contrary to the ruling *McCarroll*—that disputes about no-strike clauses were arbitral issues.

Similarly, the decisions in *Southland* and *Bruce-Allied* abrogate the *McCarroll* decision insofar as its permits the superior court to perform a peremptory gatekeeping function even when the parties have expressly conferred that function upon the arbitrator under their agreement. (*Southland, supra,* 465 U.S. at 7, 10, 79 L.Ed.2d at 10, 11-12; *Allied-Bruce, supra,* 513 U.S. at 281, 130 L.Ed.2d at 769; *McCarroll, supra,* 49 Cal.2d at pp. 65-66.)

Moreover, in *Perry v. Thomas,* 482 U.S. 483, 96 L.Ed.2d 426, 107 S.Ct. 2520, this Court specifically held that the FAA pre-empted a California statute (§ 229 of the Labor Code) which permitted the collection of wages without regard to the existence of a private international commercial arbitration agreement.

There has been a dramatic shift during the past decade by the legal community as a whole away from litigation as the principal means of resolving disputes to alternative dispute resolution ("ADR"), in particular, arbitration, especially in the business community.

This shift has been encouraged and strongly promoted by the courts in an effort to reduce caseload and more efficiently dispose of disputes. As time goes by and this movement toward ADR and away from litigation grows, the courts will begin seeing—and having to dispose of—a tremendous amount of arbitration disputes governed by the FAA, for with the fast growing use of the Internet and the rapidly shrinking global marketplace, it will soon be nearly impossible to transact any business that does not involve interstate commerce.

The International Arbitration Rules of the AAA, and the FAA will increasingly govern more and more arbitration disputes in this state; and United States citizens and people doing business in this country need to be able to contract with certainty regarding the enforceability of arbitration agreements.

Accordingly, there is a compelling need for clarity and uniformity on the issue of enforcement of private, commercial arbitration agreements governed by the FAA in California and throughout the country which necessitates this Court's review.

## *IV. REASONS FOR GRANTING THE WRIT*

### *A. The Decision by the California Supreme Court to Permit the Superior Court to Determine the Arbitrability of a Dispute Where the Parties Have Expressly Confered That Authority on the Arbitrator Pre-Empts Federal Arbitration Law in Violation of the Supremacy Clause of the United States Constitution*

#### *1. In Enacting The Federal Arbitration Act, Congress Withdrew The States' Power To Require A Judicial Forum For Resolution Of Disputes Which The Parties Agreed To Arbitrate*

"Federal law governs arbitration issues in agreements affecting interstate and foreign commerce." (*Bauhinia Corp. v. China Nat. Machinery & Equipment*, 819 F.2d 247, 249 (9th Cir. 1987); see also, *ATSA of California v. Continental Ins. Co.*, 702 F.2d 172, 175 (9th Cir. 1983).)

The FAA: (1) makes written arbitration provisions in contracts evidencing a transaction involving commerce enforceable; (2) preempts state law that seeks to invalidate arbitration agreements; and (3) prohibits state courts from applying state statutes that invalidate arbitrations. (9 U.S.C. § 2; *Southland, supra*, 465 U.S. at 15-16, 79 L.Ed.2d at 14-15; *Allied-Bruce, supra*, 513 U.S. at 272, 130 L.Ed.2d at 763.)

Section 2 of the FAA is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary.

Thus, in enacting § 2 of the FAA, Congress withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration; and created a body of federal substantive law of arbitrability, applicable to any arbitration agreement within the coverage of the Act. (*Perry v. Thomas, supra,* 482 U.S. at 489, 96 L.Ed.2d 426, 107 S.Ct. 2520, citing *Southland, supra,* 465 U.S. at 10-12, 79 L.Ed.2d 1, 104 S.Ct. 852 and *Moses H. Cone Memorial Hospital v. Mercury Construction Corp., supra,* 460 U.S. at 24, 74 L.Ed.2d 765, 103 S. Ct. 927.)

*2. This Court's Decision In* Perry v. Thomas
*Expressly Determined That A California Statute May Not Be Applied To Pre-Empt The Federal Arbitration Act*

The federal courts have, of course, original jurisdiction over actions involving the FAA. (*Perry v. Thomas, supra,* 482 U.S. 483, 96 L.Ed.2d 426, 107 S.Ct. 2520.)

In *Perry v. Thomas,* a former employee of a brokerage firm brought an action in California Superior Court against his former firm and two other employees, arising from a dispute over commissions on the sale of securities. The former employee alleged, *inter alia,* breach of a contract containing an arbitration provision, but he refused to arbitrate and the other two employees filed a petition in the Superior Court to compel arbitration under § 2 of the Federal Arbitration Act.

The former employee, opposing the petition, cited a California statute providing that actions to collect wages may be maintained without regard to the existence of any private agreement to arbitrate. The Superior Court denied the petition, holding that this Court's decision in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware,* 414 U.S. 117, 38 L.Ed.2d 348, 94

S.Ct. 383, was controlling authority to the effect that, in accordance with the California statute, actions to collect wages may be pursued without regard to private arbitration agreements.

The California Court of Appeal, Second Appellate District, affirmed, holding that the California statute was not pre-empted by the Federal Arbitration Act. The California Supreme Court denied the two employees' petition for review.

On certiorari, this Court reversed and remanded in a 7-2 decision. In an opinion by Justice Marshall, joined by Chief Justice Rehnquist and Justices Brennan, White, Blackmun, Powell and Scalia, this court determined that the California statute was in conflict with § 2 of the FAA and was, therefore, pre-empted under the Federal Constitution's Supremacy Clause.

Similarly, the appellate opinion in this action applied the McCarroll decision to defeat the parties' expressed intent to submit all disputes, including the arbitrability of a dispute, to the arbitrator, in direct conflict with section 2 of the FAA and in violation of the Supremacy Clause of the United States Constitution.

*3. The California Supreme Court's Decision Conflicts With This Court's Decisions Enforcing International Commercial Arbitration Agreements Challenged In State Court*

In *Southland, supra,* this Court held that the California Supreme Court's interpretation of the California Franchise Investment Law (C.C.P. § 31512)[2] as invalidating arbitration agreements covered by the Federal Arbitration Act was unconstitutional.

The parties in *Southland;* namely, Southland Corp. and several franchisers of 7-Eleven convenience stores, entered into a franchise agreement which provided that any controversy or claim arising thereunder would be settled by arbitration in accordance with the Rules of the American Arbitration Association. (*Id.,* 465 US at 3-4, 79 L.Ed.2d at 8.)

[2]Unless otherwise noted, all references herein to "C.C.P." shall refer to the California Code of Civil Procedure.

The franchisers filed suit in California Superior Court alleging, *inter alia,* violations of the Franchise Investment Law, and Southland petitioned to compel arbitration. The trial court refused to compel arbitration under the Franchise Investment Law, the Court of Appeal reversed, and this Court reversed the Court of Appeal, interpreting the Franchise Investment Law as requiring judicial consideration of all claims brought thereunder and refusing to enforce the parties' agreement to arbitrate.

The *Southland* Court determined that the interpretation of the Franchise Investment Law as requiring judicial consideration of claims, rather than arbitration as agreed by the parties, directly conflicted with section 2 of the Federal Arbitration Act and violated the Supremacy Clause of the United States Constitution. (*Southland, supra,* 465 U.S. at 10-11, 16, 79 L.Ed.2d at 11-12, 15.)

The *Southland* Court stated that the effect of the California Supreme Court's refusal to enforce the arbitration agreement between the parties was to *"nullify a valid contract made by private parties under which they agreed to submit all contract disputes to final, binding arbitration"*; and further opined that *"[c]ontracts to arbitrate are not to be avoided by allowing one party to ignore the contract and resort to the courts. Such a course could lead to prolonged litigation, one of the very risks the parties, by contracting for arbitration, sought to eliminate."* [Emphasis added.] (*Id.,* 465 U.S. at 7, 79 L.Ed.2d at 10.)

Similarly, the Court of Appeal's refusal to enforce the arbitration agreement between the parties herein nullifies a valid contract made by private parties under which they agreed to submit all contract disputes to final, binding arbitration in contravention of federal law.

In *Allied-Bruce,* this Court considered a state court dispute concerning the enforceability of a contract's written arbitration clause. In concluding that the Alabama Supreme Court had improperly applied the state's antiarbitration statute to preclude enforcement of the arbitration clause, this Court held that the FAA reaches to the limits of Congress' Commerce Clause power and applies to actions brought in state court

when the transaction involves interstate commerce, whether or not the parties contemplated an interstate connection[3]. (*Allied-Bruce, supra,* 513 U.S. at 277, 130 L.Ed.2d at 763.)

This Court further stated:

> "[w]hat states may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal 'footing', directly contrary to the Act's language and Congress' intent. See *Volt Information Sciences, Inc.* 489 U.S. at 474, 103 L.Ed.2d 488, 109 S.Ct. 1248.)" (*Allied-Bruce, supra,* 513 U.S. at 281, 130 L.Ed.2d at 769, 115 S.Ct. 834.)

In the instant action, there can be no doubt that the parties' transaction involved interstate commerce; and that the parties expressly agreed that any and all disputes would be resolved in accordance with the International Arbitration Rules of the AAA. (CT 139, ll. 7-12; 145, 151.)

Therefore, the application of the *McCarroll* decision by the Court of Appeal affirming the San Mateo County Superior Court's authority to determine the arbitrability of the parties' dispute, when Petitioners and Respondent expressly agreed to confer that power upon the arbitrator, directly conflicts with the FAA, the Supremacy Clause of the United States Constitution, the *Southland* decision and the *Allied Bruce* decision, necessitating review by this Court.

### *B. The* McCarroll *Holdings Creates a Peremptory Gatekeeping Exceptions to Enforcement of Arbitration Agreements Which is Not Authorized by Federal Law*

The International Arbitration Rules of the AAA are based on the UNCITRAL (United Nations Commission on International Trade Law) model rules. Both those model rules, and the

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[3] In this action, there is no dispute regarding an interstate connection since the parties expressly agreed to be governed by the International Arbitration Rules of the AAA and, necessarily, the FAA (CT 145, 151.)

AAA International Rules, are patently clear regarding the jurisdiction of the arbitrator when parties have embedded those rules in their underlying agreement. (International Arbitration Rules of the AAA, Articles 15.1, 15.3, CT 199-200.)

In addition, California has an International Disputes Resolution Statute (the "International Statute") that is based on UNCITRAL model law. That statute is found in Title 9.3 of the California Code of Civil Procedure (§§ 1297.11-1297.432).

C.C.P. § 1297.161 *reiterates the same rule reserving the power to determine jurisdiction to the arbitrator;* and C.C.P. § 1297.166 requires an objecting party to *first* submit a jurisdictional dispute to the arbitrator *before* seeking relief from the courts.

Pursuant to C.C.P. § 1297.13 of the International Statute, the underlying transaction in this matter is international in that (i) the parties to the Agreement have their places of business in different states; (ii) the parties, by incorporating the International Rules of the AAA have evidenced that the subject matter of the Agreement relates to commercial interests in more than one state; and (iii) the subject matter of the Agreement is related to commercial interests in more than one state.

C.C.P. § 1297.51 of the International Statute further mandates that in matters governed by Title 9.3, *no court shall intervene* except when so provided by Code of Civil Procedure section 1297.11-1297.432), or by applicable federal law.

### *1. The Parties Expressly Adopted Both The International Arbitration Rules And Title 9.3 Of The Code Of Civil Procedure, Leaving No Doubt As To Their Intent To Submit All Disputes To Arbitration*

In the Agreement, the parties expressly adopt *both* the International Arbitration Rules of the AAA and, notably, the International Statute, as reiterated below:

> "4. *Arbitration.* The parties to this Agreement have submitted all disputes between them for settlement by arbitration under the authority of J.A.M.S./ENDISPUTE, San Francisco, California. *Said arbitration is deemed to be private, binding, international arbitration as provided by Title 9.3 of the California Code of Civil Procedure.* The parties hereby confirm their agreement to submit their disputes to arbitration and that this confirmation constitutes a written arbitration agreement. The parties hereby confirm their agreement to the appointment of the Hon. Harry Low as sole arbitrator. . . [Emphasis added]. (CT 145, par. 4.)
>
> "19. *Arbitration.* In the event of any dispute relating to or arising out of this agreement, the *exclusive forum* for resolution of any such dispute *shall* be by arbitration in San Francisco under the authority of JAMS/ENDISPUTE in accordance with the International Rules of the American Arbitration Association." [Emphasis added]. (CT 151, par. 19.)

Under California law, the rules selected by the parties to govern their arbitration is sufficient evidence of a "clear and unmistakable" intent to submit disputes regarding the arbitrability of a claim to arbitration:

> "The arbitrator's power to determine arbitrability might also be derived from the rules selected by the parties in their arbitration clause. For example, AAA Commercial Dispute Resolution Procedures expressly give the arbitrator power to determine the arbitrability of disputes, including the scope, validity, or enforceability of the arbitration agreement. [AAA Commercial Dispute Resolution Procedures, Rule R-8.]"

> "JAMS Comprehensive Arbitration Rules and Procedures, Rule 10, is similar. Reference to one of these rules in the arbitration clause effectively makes the rule part of the agreement. [See *First Options of Chicago, Inc. v. Kaplan, supra,* 514 U.S. at 944, 115 S.Ct. at 1925]" (Knight, Fannin, Chernick & Halderman, CAL. PRAC. GUIDE: ALTERNATIVE DISPUTE RESOLUTION (The Rutter Group 1999) §5:214.4, pp. 5-81 to 5-82.)

Thus, there can be no stronger objective evidence of both Petitioners' and Respondent's intent—as expressed in the Agreement—to submit all disputes regarding jurisdiction to the arbitrator, than their express adoption of the International Arbitration Rules of the AAA and Title 9.3 of the California Code of Civil Procedure.

In *First Options of Chicago v. Kaplan, supra,* 514 U.S. at 944, 131 L.Ed.2d at 994-994, this Court held that the question of who has primary power to decide arbitrability turns upon what the parties agreed to, since a party can only be forced to arbitrate those issues it specifically agreed to arbitrate. In deciding whether the parties agreed to arbitrate arbitrability, the courts should apply ordinary state law contract principles that govern formation of contracts. (*Id.,* 514 U.S. at 844; 131 L.Ed.2d at 993.)

In *First Options,* as in the case at bar, the relevant state law requires the court to see whether the parties objectively revealed an intent to submit the arbitrability issue to arbitration. (See Civil Code section 1636; *Brant v. California Dairies,* 4 Cal.2d 128, 133, 48 P.2d 13 (1935).)

As noted above, the selection of the International Arbitration Rules and Title 9.3 of the Code of Civil Procedure leaves no doubt as to the parties' intent to submit disputes regarding arbitrability to arbitration—and the appellate court's application of the *McCarroll* holding to defeat the parties' intent is contrary to federal and state law and must be reversed.

*2. The* McCarroll *Holding Should Be Limited To Its Facts Which Are Distinguishable From Those In The Case At Bar*

The Court of Appeal relied upon the California Supreme Court's decision in the *McCarroll* case in affirming the Judgment. In so ruling, the appellate court cited the following passage in the *McCarroll* decision:

> "The arbitrability of a dispute may itself be subject to arbitration if the parties have so provided in their contract. In this situation the court should stay proceedings pending the arbiter's determination of his own jurisdiction *unless it is clear that the claim of arbitrability is wholly groundless."* [Italics added by appellate court] See Appendix A-6, quoting *McCarroll,* 49 Cal.2d at 65.)

Federal law, however, provides no such exception to enforcement of arbitration agreements governed by the FAA. Indeed, as noted above, the International Arbitration Rules (in particular Articles 15.1 and 15.3) provide the exact opposite—that all disputes, including disputes regarding arbitrability, be submitted to arbitration.

In *McCarroll,* the court's entire analysis was premised upon the scope and clarity of the parties' agreement and the extent to which it called for any court involvement in questions of arbitrability and jurisdiction. At the outset, the *McCarroll* Court looked at the arbitration clause and *based on its lack of clarity as to jurisdiction and arbitration,* determined that the parties had not agreed to allow the arbitrator to decide his own jurisdiction.

In decided contrast to the arbitration clause at issue in the parties' Agreement, the arbitration clause in *McCarroll* provided for grievances to be funneled through a series of personnel before even getting to an arbitrator, and the parties agreed to present their disputes to a multitude of different entities: a "craft steward", "special representative", "contractor", "Joint Contractor Board", "Joint Arbitration Committee", and finally, if the dispute remained unresolved, to an arbiter. (*McCarroll, supra,* 49 Cal.2d at 65.)

Given the long succession of decision-makers, the *McCarroll* Court determined that the parties had failed to agree that

the arbitrator had the power to decide his own jurisdiction. It was only because the parties had not clearly stated an intent to permit the arbitrator to decide jurisdiction—*"there is no indication in the present contract that the parties intended any such result"* [i.e., to confer the power of determining jurisdiction upon the arbitrator]—that the *McCarroll* Court assumed responsibility for determining jurisdiction. Thus, the *McCarroll* holding should be expressly limited to situations where the parties have not agreed upon who decides jurisdiction. (*Id.*, at 65-66.)

The facts in the instant action could not be more distinguishable. Appellants and Respondent did agree—at Respondent's insistence—that the arbitrator should decide jurisdiction by selecting the International Arbitration Rules of the AAA and the International Statute to govern their disputes. In accordance therewith, the Court of Appeal's decision is contrary to federal law insofar as it permits superior courts to refuse to enforce arbitration agreements where the superior court makes a peremptory determination that there are no arbitral issues.

### *3. The Ninth Circuit Of The United States Court of Appeals Recently Issued A Decision Upholding The Right Of Private Parties To Contract For Arbitration*

This issue is extremely timely, as evidenced by this Court's grant of review in the *Circuit City Stores, supra,* and *Green Tree, supra,* cases for the current term; and the Ninth Circuit's recent decision in *Portland General Electric Company v. U.S. Bank Trust National Association* (July 18, 2000) 2000 Daily Journal D.A.R. 7819.

The *Portland* case involved a dispute regarding whether Oregon law or the FAA governed a challenge to a final appraisal decision issued pursuant to a commercial contract. The facts are distinguishable from those in the instant appeal, but the Ninth Circuit's holding that courts must keep sacrosanct the right to contract for arbitration and must strictly enforce those rights as written, is applicable to this case. (*Portland, supra,* 2000 Daily Journal D.A.R. at 7821.)

The central issue in *Portland* was whether the district court had properly interpreted the parties' agreed appraisal procedure as an agreement to arbitrate, based on its erroneous conclusion that a prior Ninth Circuit decision [*Raytheon Co. v. Rheem Manufacturing Co.*, 322 F.2d 173 (1963)] had held that a contractually mandated appraisal is the equivalent of an arbitration subject to the FAA. (*Id.*)

In distinguishing the *Raytheon* case, the Ninth Circuit reiterated the principle that courts play a limited role in construing appraisal agreements, serving only to enforce the parties' bargain, not "to add gloss to the parties' own language". (*Id.*)

In analyzing whether the FAA applied to the Portland agreement, the Court acknowledged that "[t]he FAA governs any written provision in a *'contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract.'* 9 U.S.C. § 2." [Emphasis added.] (*Id.*, at 7820.)

The Court then looked to the FAA for a definition of "appraisal", but finding none, stated: *"[a]lthough the FAA does not provide any guidance on definitions, it does direct us to the contract itself."* [Emphasis added.] (*Id.*, at 7820.)

In the instant action, of course, there is no dispute as to the applicability of the FAA because the parties expressly agreed to arbitrate all disputes in accordance with the International Arbitration Rules of the AAA, which are governed by the FAA.

However, the general rule that the FAA governs all contracts evidencing a transaction involving commerce, and further requires the courts to enforce an arbitration agreement as written, is relevant to this case.

> "The function of the court is very limited when the parties have agreed to submit all questions of contract interpretation to the arbitrator. It is confined to ascertaining whether the party seeking arbitration is making a claim which on its face is governed by the contract. Whether the moving party is right or wrong is a question of contract interpretation for

> the arbitrator. In these circumstances the moving party should not be deprived of the arbitrator's judgment, when it was his judgment and all that it connotes that was bargained for." (*United Steelworkers v. American Mfg. Co.*, 363 U.S. 564, 80 S.CT. 1343, 4 L.Ed.2d 1403 (1960).)

That is precisely what Petitioners bargained for by expressly adopting the International Arbitration Rules of the AAA in their arbitration agreement—the arbitrator's judgment—and federal law mandates that the parties' intent to arbitrate be enforced.

*C. The Decision by the California Supreme Court to Permit the Foreclosure and Sale of Petitioners' Home Without the Bargained for Notice Violates the Due Process Clause of the Fourteenth Amendment.*

The Fourteenth Amendment of the United States Constitution prohibits rendering a judgment depriving a person of property in any contested proceeding without constitutional guarantees of due process. (*D.H. Overmyer Co. v. Frick Co.*, 405 U.S. 174, 185-186, 31 L. Ed. 2d 124, 92 S.Ct. 775; *Lambert v. California*, 355 U.S. 225, 228, 2 L.Ed.2d 228, 78 S.Ct. 240, reh den 355 U.S. 937, 2 L.Ed.2d 419, 78 S.Ct. 410 (1985).)

The Judgment herein was entered ex parte, without the requisite hearing on the merits guaranteeing Petitioners of the constitutional protection of due process. Thus, at a minimum, there should have been a threshold hearing on the issue of the court's jurisdiction to even conduct an evidentiary hearing and enter judgment prior to the conclusion of the arbitration commenced by Appellants on October 2, 1999.

Further, under California law any "application", such as Respondent's application for ex parte application for entry of judgment, is the same as a motion. (C.C.P. § 1003.)

A motion shall be upon all grounds stated in the written notice, and is deemed to have been made and be pending before the court for all purposes upon the due service and filing of the motion, but this shall not deprive party of a hearing on a motion to which he is otherwise entitled. (C.C.P. § 1005.5.)

It is worth repeating that, in this case, the superior court did not hear oral argument before entering an ex parte judgment of foreclosure and order of sale of Petitioners' home of more than twenty-two years.

Under California Code of Civil Procedure § 166(a), only certain specified motions may be heard in chambers, such as motions to vacate a verdict or for new trial (C.C.P. § 657); motions to vacate a judgment (C.C.P. § 663); all uncontested actions or proceedings; ex parte applications; and motions to tax costs of enforcing a judgment.

Notably, motions to enter judgment by stipulation under Code of Civil Procedure § 664.6 are not included within the motions permitted to be heard in chambers.

The "hearing" on Respondent's ex parte application herein consisted of a research clerk shuttling statements of counsel back and forth to the Judge who was at all times in chambers. The Judge signed the order entering judgment against Petitioners while in chambers.

Thus, the Superior Court effectively deprived Petitioners of their right to make oral argument, leaving all emphasis, nuance and attention to the voluminous and complex details of this case to the research clerk who communicated Petitioners' argument to the Judge in chambers.

As noted in by the Court of Appeal in *Mediterranean Co. v. State Farm Fire & Casualty Company,* 66 Cal.App.4th 257, 264, 77 Cal.Rptr.2d 781 (1998), a hearing affords litigants their *only opportunity* to orally argue their case and to respond to the court's inquiries through the give and take of questioning.

As one leading jurist aptly stated: "An oral argument is as different from a brief as a love song is from a novel. It is an opportunity to go straight to the heart!" [exclamation point in original text]. (*Mediterranean Co. v. State Farm Fire & Casualty Company, supra,* 66 Cal.App.4th at 264, quoting *Kaufman, Appellate Advocacy in the Federal Courts,* 79 F.R.D. 165, 171 (1977).)

In the case at bar, the love song was sung to the clerk who sang it to the judge. Something was lost in the translation.

The case of *Hobbs v. Weiss,* 73 Cal.App. 4th 76, 77, 86 Cal.Rptr.2d 146 (1999), (199 Daily Journal D.A.R. 6583) decided by the Court of Appeal emphatically re-states the point clearly made by the Court in the *Mediterranean* case:

> **"In *Mediterranean Construction* we expressed our frustration with law and motion judges who "refuse to hold oral hearings on critical pre-trial matters of considerable significance to the parties . . . fair warning: Both written and oral argument are complementary parts of good judging and elemental due process."** *(Id.)*

The circumstances here are more dire than those in the *Hobbs* case, where a pre-trial writ of attachment was at issue, and more akin to those at issue in the *Mediterranean* case, where summary judgment was at issue.

The entry of the Judgment without a hearing by the superior court resulted in the loss of Petitioners' home by foreclosure; the forfeiture of penalty damages in the amount of $2,300.000.00 [i.e. the full sum of $7,500,000.00 became due upon entry of the Judgement]; and the loss of equity in the sum of eight million ($8,000,000.00) dollars.

In the Agreement, Petitioners bargained for—and Respondent agreed—to submit all disputes to arbitration before Respondent could enforce any of the remedies under the Agreement, specifically entry of the Judgment on an ex parte basis. (CT 151.)

Thus, the dictates of due process hold that there should have been a threshold hearing on the arbitrability of the parties' disputed tender before Respondent could lawfully seek entry of the Judgment in the superior court. Moreover, that is what Petitioners bargained for—a hearing, however brief, on the merits of any dispute—before Respondent could enforce the drastic remedies provided in the Agreement. Petitioners did not receive their bargained for notice, and the ex parte Judgment violates Petitioners' constitutionally guaranteed right of due process.

## *IV. CONCLUSION*

A writ of certiorari should issue, since the decision of the California Supreme Court relied upon by the Court of Appeal in affirming the Judgment conflicts with the decisions of this Court regarding enforceability of the FAA in state courts.

The questions presented on review are serious, important and timely. The California Supreme Court's decision opens the way for pre-empting federal law in favor of state law even though there is an express congressional declaration favoring arbitration notwithstanding any state substantive or procedural policies.

For the reasons stated Petitioners respectfully request this Court to grant the writ of certiorari.

Respectfully submitted,

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*Counsel of Record for Petitioners*

Dated: October 19, 2000

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**APPENDIX A**

NO. A085195

IN THE

# Court of Appeals of the State of California
# First Appellate District
# Division Four

## San Mateo County
## Superior Court
## No. 391951

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FIRST PACIFIC BANK LIMITED,
*Plaintiff and Respondent,*

*v.*

THE BVY GROUP, INC. ET AL.,
*Defendants and Appellants.*

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The BVY Group, Inc., Benedicto Yujuico, and Teresita Yujuico appeal from a judgment for judicial foreclosure entered on the ex parte application of respondent First Pacific Bank Limited. Appellants contend that: respondent breached the parties' settlement agreement by applying for entry of judgment; the court lacked jurisdiction to enter the judgment; and their due process rights were violated in connection with the entry of judgment. We affirm.

## *FACTS*

This action was filed by respondent for judicial foreclosure of property securing indebtedness owed by appellants. While the action was pending, the parties entered into a settlement agreement dated as of August 1, 1997. Attached to the settlement were an agreement for binding arbitration between the

parties, and an arbitration award setting forth the parties' agreements that: appellants owed respondent $7,500,000 as of August 1, 1997; appellants' debt was secured by a property the Yujuicos owned in Atherton; the Atherton property could be sold to satisfy the debt; and appellants would be liable for any deficiency after that sale. Also attached to the settlement were a stipulation for enforcement of the arbitration award, and a stipulated judgment thereon for judicial foreclosure. In the settlement agreement, appellants agreed to pay respondent $5,200,000 in installments ending on August 15, 1998. In the event of a default in the payments, the settlement agreement authorized respondent to pursue various remedies without further notice to appellants, including entry of the stipulated judgment on the arbitration award.

The settlement agreement included the following arbitration provision: "In the event of any dispute relating to or arising out of this Agreement, the exclusive forum for resolution of any such dispute shall be by arbitration in San Francisco, California under the authority of J.A.M.S./ENDISPUTE in accordance with the International Arbitration rules of the American Arbitration Association."

In February 1998 the parties executed an amendment to the settlement agreement which provided for a revised payment schedule extending the final payment to September 15, 1999. Benedicto Yujuico's father, Jesus Yujuico, executed a guaranty for the amount of the remaining payments ($2.2 million) and a consent to the amendment. The settlement agreement had recited that: respondent had made loans to Standard Fund International Limited (SFIL), a corporation owned by Jesus Yujuico, as set forth in agreement between respondent, SFIL, Jesus Yujuico and Conifer Properties, Inc.; and Jesus Yujuico had joined appellants and other parties in a cross-complaint against respondent in the judicial foreclosure action. However, Jesus Yujuico was not a signatory to the settlement agreement or the amendment thereto.

Under the settlement agreement as amended, appellants owed respondent a payment of $450,000, with interest, on September 15, 1998. Respondent's Vice President Peter Choy received a letter dated September 9, 1998, from Lito Bermundo, who had previously signed correspondence to respondent as Jesus Yujuico's financial consultant. The letter noted Choy's "negative reply to our letter request dated August 30, 1998 which basically pleads for a one year extension of principal payments for both the SFIL and BVY Group outstanding obligations," and "submit[ted] another proposal for your consideration as follows: . . .

> We have found a buyer for the BVY Note with the following terms: $100,000 downpayment and the balance to be paid within 12 months or earlier. Interest on the account will be paid quarterly." The letter added: "We realize that you can deny our request and instead foreclose the BVY Group collateral." Respondent rejected this proposal by letter dated September 10, 1998.

On September 16, 1998, Choy wrote appellants and Jesus Yujuico a letter which noted that the September 15 payment had not been received and threatened legal action as provided in the settlement agreement. That same day, Bermundo wrote Choy and proposed, with emphasis in the original, that Jesus Yujuico would "use the funds earmarked from the down payment of the Conifer refinancing to instead purchase the BVY Note from the bank.[1] *He proposes a down payment of $450,000 and the balance to be paid in full by March 15, 1999.* (The original payment term is $450,000 on September 15, 1998 and $850,000 each on March 15, 1999 and Sept. 1999.)[2] *In addition, he proposes to pay legal costs of undertaking the documentation for the purchase of the note, plus a $10,000 fee to cover any administration costs to implement our proposal."*

---

[1] The "BVY Note" apparently referred to appellants' debt under the amended settlement agreement.

[2] This apparent reference to the terms of the amended settlement agreement overstated the $650,000 payments due under that agreement in Marchand September 1999.

On September 17, 1998, Choy wrote Jesus Yujuico and advised that respondent "may consider assigning its entire interest in the BVY loan to any investor on the basis that the Bank receives immediate good funds to satisfactor[il]y discharge full amount of the indebtedness under the BVY loan facility. We regret that your latest proposal of defer and partial payment is not acceptable to us." The letter reiterated the demand for immediate payment of the September 15 installment. On September 30, 1998, respondent's counsel wrote appellants and stated that respondent would exercise its legal remedies if the September 15 payment was not received by October 5.

Appellants' counsel prepared a demand for arbitration dated October 2, 1998, stating that "a dispute has arisen concerning the rights and obligations of the parties under the [settlement] Agreement, namely that First Pacific asserts that BVY has defaulted in its obligations under the Agreement and BVY asserts that it tendered performance which was improperly refused by First Pacific." In a letter dated October 7, 1998, respondent rejected appellants' assertion "that there is any basis whatsoever for further arbitration before J.A.M.S." On October 8, respondent's counsel notified appellants' counsel that respondent would be presenting an ex parte application to the superior court the next day for entry of a stipulated judgment in accordance with the settlement agreement.

Appellants appeared at the October 9 hearing with a memorandum in opposition to the application and presented arguments to the court's research attorney, who conveyed them to the judge. The judge asked appellants' counsel, through the research attorney, whether any provision of the amended settlement agreement obligated respondent to accept a third-party offer like the one made by Jesus Yujuico.

Judgment was entered as requested authorizing respondent to foreclose on the Atherton property and recover any deficiency following the sale. Appellants' motion to vacate the judgment was denied and this appeal ensued.

## *DISCUSSION*

Appellants contend that respondent breached the settlement agreement by seeking entry of judgment before the issue of their alleged tender of performance was arbitrated. Appellants note that they waived various legal rights in the settlement agreement, and maintain that the provision for arbitration of disputes before these "draconian waivers could be enforced" was at "the very heart of the consideration" for the agreement. Appellants submit that once they demanded arbitration, the only way respondent could object to the demand was to assert that objection in the arbitration. They observe that the AAA International Arbitration Rules provide for objections to the tribunal's jurisdiction. (Art. 15.3; see also Art. 15.1, Code Civ. Proc., § 1297.161 [tribunal may rule on its own jurisdiction].)

Whether the application for entry of judgment was a breach of the settlement agreement hinges on appellants' claim that respondent's refusal to accept Jesus Yujuico's offer created a "dispute relating to or arising out of" the agreement within the meaning of the arbitration clause. If there was no arbitrable dispute then respondent did not breach the agreement by obtaining the judgment, and the arbitration demand was an attempt to deprive respondent of *its* rights under the agreement.

Appellants assert that the court lacked jurisdiction to rule on the merits of their arbitration demand or enter judgment while the arbitration proceeding was pending. Appellants take the position that once they identified a "dispute" under the settlement agreement and demanded arbitration, the court was powerless to act until that alleged dispute was resolved by an arbitrator. This position relieves appellants of any need to show that Jesus Yujuico's offer was a valid tender of performance under the settlement agreement. Appellants maintain that "[w]hether [they] did or did not make valid tender, or whether [they] merely offered to modify the terms of the existing contract, are not the issues before this Court."

Appellant's breach of contract and lack of jurisdiction arguments are contrary to the law as stated in *McCarroll v. L.A. County etc. Carpenters* (1957) 49 Cal.2d 45: "The arbitrability of a dispute may itself be subject to arbitration if the parties have so provided in their contract. In this situation the court should stay proceedings pending the arbiter's determination of his own jurisdiction *unless it is clear that the claim of arbitrability is wholly groundless.*" (*Id.* at p. 65 [italics added].)[3] The emphasized language confirms the jurisdiction of the court to determine whether there is any substance to an arbitration demand, and the right of a party to an arbitration agreement to seek such a determination.

As respondent points out, appellants' theory would enable them to indefinitely postpone the entry of judgment with a series of sham arbitration demands. To quote from respondent's brief: "Under [appellants'] theory, they could fail to make a payment and file an arbitration demand, alleging that payment was excused because the sky was gray on the payment date. They could then successfully argue that [respondent] was in breach by seeking entry of the [stipulated judgement] on the ground that their 'gray sky' 'excuse' for nonpayment gave rise to a dispute that 'arose out of' the [arbitration agreement] and had to be arbitrated, and that only an arbitrator could determine its arbitrability.

> Once that sham claim of arbitrability was resolved, [appellants] could manufacture yet another purportedly arbitrable dispute—claiming, for example, that payment was not due because the sun set before 7 p.m. on the payment date."

This case thus illustrates why it is sound policy to reserve a limited "gatekeeping" function for the court, even when the parties have agreed to arbitrate the issue of the arbitrator's jurisdiction. If courts cannot determine whether claims are at

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[3] The holding of the McCarroll case on another point was abrogated by *Drake Bakeries v. Bakery Workers* (1962) 370 U.S. 254, 257. *(Charles J. Rounds Co. v. Joint Council of Teamsters* (1971) 4 Cal.3d 888, 893.)

least arguably subject to arbitration, parties can be subjected to arbitration proceedings for which they clearly have not bargained.

Accordingly, we reject the breach of contract and lack of jurisdiction arguments. Respondent had the right to test the merits of the arbitration demand by seeking the entry of judgment, and the court had the power to determine that the demand was untenable, as it implicitly found by entering judgment over appellants' objection.[4]

Appellants' remaining argument is that the ex parte procedure by which judgment was entered deprived them of due process. However, parties may waive their due process rights in connection with entry of a stipulated judgment (e.g., *County of Ventura v. Tillett* (1982) 133 Cal.App.3d 105, 112-113, disapproved on another point in *County of Los Angeles v. Soto* (1984) 35 Cal.3d 483), and appellants did so here when they agreed that the stipulated judgment could be filed "without further notice" if they failed to make a scheduled payment. Despite this agreement, respondent notified appellants of the hearing on the application for entry of judgment, and the record shows that appellants were able to fully present their arguments at that hearing and in their motion to vacate the judgment.

Appellants contend that they were wrongfully deprived of oral argument before the judge at the hearing on the application, "leaving all emphasis, nuance and attention to the voluminous and complex details of this case to the research clerk who communicated Appellants' argument to the Judge in chambers ...

> As one leading jurist aptly stated: "'An oral argument is as different from a brief as a love song is from a novel.'" . . .

---

[4] Since appellants do not attempt to justify their claim that there was a valid tender under the settlement agreement, we need not reach that issue.

In the case at bar, the love song was sung to the clerk who sang it to the judge. Something was lost in the translation." However, appellants received more process than they agreed to accept.

*DISPOSITION*

The judgment is affirmed with costs to respondent.

Hanlon, P.J.

We concur:

Poché, J.

Sepulveda, J.

(A085195, First Pacific Bank v. The BVY Group et al.)

**APPENDIX B**

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The BVY Group, et al.

SUPERIOR COURT OF CALIFORNIA
COUNTY OF SAN MATEO

FIRST PACIFIC BANK LIMITED, a Hong Kong banking corporation,

Plaintiff,

vs.

THE BVY GROUP, a California Corporation, et al.,

Defendants.

_____/

No. 391951

[PROPOSED] JUDGMENT OF FORECLOSURE AND ORDER OF SALE

Date: October 9, 1998
Time: 2:00 p.m.
Dept. 10
Trial Date: None Set

THE BVY GROUP, a California corporation, et al.,

Cross-Complainants,

vs.

FIRST PACIFIC BANK LIMITED, a Hong Kong banking corporation, et al.

Cross-Defendants.

_____/

WHEREAS, plaintiff First Pacific Bank, Ltd. appeared by Crosby, Heafey, Roach & May, Professional Corporation, counsel; cross-complainants the BVY Group, Inc., Benedicto V. Yujuico and Teresita M. Yujuico appeared by Tatro, Coffino, Zeavin, Bloomgarden, LLP, counsel.

WHEREAS, the parties agreed to settle this action by arbitration; an arbitration award was made by the Honorable Harry W. Low, Arbitrator, and consented to by the parties;

WHEREAS, the parties have entered a Stipulation through which Cross-Complainants The BVY Group, Inc., Benedicto V. Yujuico and Teresita M. Yujuico have stipulated to confirmation of the arbitration award and entry of the instant Judgment of Foreclosure and Order of Sale;

IT IS ADJUDGED, ORDERED, AND DECREED that:

1. The arbitration Award attached hereto is confirmed.

2. There are now due and owing to plaintiff First Pacific Bank Limited from cross-complainants The BVY Group, Inc., Benedicto V. Yujuico and Teresita M. Yujuico, the following sums, secured by: (1) a Deed of Trust dated on or about November 8, 1989, executed by the Yujuicos as trustor, to U.F. Service Corporation, as trustee, for plaintiff First Pacific Bank, Ltd. as beneficiary, recorded on November 20, 1989, as Document No. 89157320 in the Official Records in the Office of the Recorder of San Mateo County, California, constituting a lien on the real property hereinafter described: the sum of $7,500,000, the repayment of which is guaranteed by the Yujuicos.

3. The real property hereinafter described, or so much of it as may be necessary, is to be sold in the manner prescribed by law by the levying officer of San Mateo County, California, on application for issuance of a writ of sale to the levying officer. Any party to this action may be a purchaser at the sale.

4. From the proceeds of the sale, the levying officer shall deduct the expenses for the levy and sale, and shall then pay to plaintiff the sums adjudged due, together with interest from the date of this judgment at an annual rate equal to seven (7) percent.

5. If any surplus remains after making these payments, it shall be paid by the levying officer to cross-complainants The BVY Group, Inc., Benedicto V. Yujuico and Teresita M. Yujuico.

6. Cross-complainants The BVY Group, Inc., Benedicto V. Yujuico and Teresita M. Yujuico, are liable for payment of the sums secured by the Deeds of Trust and a deficiency judgment may be ordered against them following proceedings prescribed by law, and cross-complainants Benedicto V. Yujuico and Teresita M. Yujuico have personally guaranteed repayment of such sum. The Court retains jurisdiction to determine the amount of the deficiency, if any, and to render a money judgment on proper application therefore against BVY hereunder or Benedicto V. Yujuico and Teresita M. Yujuico under their Guaranty.

7. A deficiency judgment not being waived or prohibited, the property is to be sold; provided, however, that BVY has by separate agreement waived its rights of redemption provided in Sections 729.010 to 729.090, inclusive, of the Code of Civil Procedure.

8. From and after the delivery of the Deeds by the levying officer to the purchaser at the sale, cross-complainants The BVY Group, Inc., Benedicto V. Yujuico and Teresita M. Yujuico and all persons claiming under them, and all persons having liens subsequent to the Deeds of Trust by any judgment on the real property hereinafter described, and their personal representatives, and all persons claiming under them, and all persons claiming to have acquired any estate or interest in the property subsequent to the filing of notice of the pendency of this action with the county recorder are forever barred and foreclosed from all equity of redemption in, and claim to, the property and every part thereof.

9. The property which is the subject of the judgment and order is situated in San Mateo County, California, and is described as follows:

(1) Parcel "B", as shown on that certain map entitled "PARCEL MAP BEING A SUBDIVISION OF LOT 8B AND A PORTION OF LOT 3A, MAP OF QUILLOTA TRACT FILED IN VOLUME D OF MAPS AT PAGE 32, SAN MATEO COUNTY RECORDS, TOWN OF ATHERTON, SAN MATEO COUNTY, CALIFORNIA", which map was filed in the office of the County Recorder of San Mateo County, State of California, on August 2, 1971, in Book 13 of Parcel Maps at Page 20.

DATED: _____

_____
JUDGE OF THE SUPERIOR COURT

Court of Appeal, First Appellate District, Division Four
No. A085195

S090027

**IN THE SUPREME COURT OF CALIFORNIA**

En Banc

---

FIRST PACIFIC BANK LIMITED, Plaintiff and Respondent,

v.

THE BVY GROUP INC., et al., Defendant and Appellants.

---

Petition for review DENIED.

GEORGE
Chief Justice

No. 00-631

FILED
NOV 13 2000
CLERK

In The

# Supreme Court of the United States

BENEDICTO V. YUJUICO, et al.,

*Petitioners,*

v.

FIRST PACIFIC BANK LIMITED,

*Respondent.*

**On Petition For A Writ Of Certiorari To The California Court Of Appeal For The First Appellate District, Division Four**

## RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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## QUESTION PRESENTED

Whether the California Court of Appeal's unpublished decision correctly affirmed the trial court's judgment of foreclosure, where Petitioners:

(1) To settle foreclosure litigation, stipulated to the entry of judgment for valuable consideration while represented by counsel;

(2) Thereafter sought to delay or avoid entry of judgment by manufacturing an arbitration demand that, after giving petitioners notice and the opportunity to be heard, the state courts found to be "wholly groundless";

(3) Raised no question arising under the Federal Arbitration Act until after the Court of Appeal issued its unpublished opinion; and

(4) Did not raise their present due process claim in the California Supreme Court.

## CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6, Respondent First Pacific Bank Limited represents that it is a foreign corporation owned 100 percent by FEB (1989) Limited, which in turn is owned 100 percent by FPB Bank Holding Company Limited, which in turn is owned 51 percent by FPMF Limited, 24 percent by MIMET FOTIC Investment Limited and 25 percent by the public. All of the above are foreign corporations, based either in Bermuda or in Hong Kong.

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# I

## PRELIMINARY STATEMENT

Certiorari is reserved for cases that present groundbreaking issues of broad national significance that the petitioning party has properly raised in the courts below. This case does not fall into that category.

Petitioners have raised two issues for review: (1) whether the Federal Arbitration Act prevents a trial court from declining to refer a "wholly groundless" claim of arbitrability to arbitration; and (2) whether the entry of a stipulated judgment after petitioners waived their right to notice and an opportunity to object to its entry (and after petitioners participated in the entry-of-judgment procedure and were heard on their motion to vacate the judgment) violated due process. Neither issue is appropriate for review, for two reasons.

First, Petitioners failed to raise both of these issues in the state court proceedings in a timely and proper fashion, as this Court's decisions require. Petitioners did not raise their first issue until after the California Court of Appeal filed its opinion. And they did not raise their second issue when they sought review of that opinion in the California Supreme Court. Petitioners nowhere attempt to explain these failings because they cannot. These omissions alone are grounds for denying their petition.

Second, the Court of Appeal's unpublished opinion resolved questions of state law that do not implicate any important national policy, let alone federal questions of any significance. Petitioners are simply wrong in asserting otherwise.

Petitioners' first claim involves an invented conflict between California and federal law concerning a court's obligation to refer the arbitrability of a dispute to arbitration. In fact, the federal and state courts are in full accord on the rule that the Court of Appeal applied – that a trial court has the right, notwithstanding the Federal Arbitration Act, to perform a limited "gatekeeping" function and refuse to send to arbitration "wholly groundless" claims of arbitrability. It is not surprising that when Petitioners *did* raise this claim below (albeit belatedly), the lower courts rejected it. Thus, review would accomplish nothing because the lower courts were correct, and there is no conflict to resolve.

Petitioners' second claim involves a purported due process violation in the entry of a stipulated judgment. But while represented by the counsel of their choice, Petitioners waived their due process rights when they stipulated to the judgment. Even so, they were given notice and were heard – both before and after the judgment was entered. Petitioners were apparently satisfied with the Court of Appeal's rejection of their due process claim, as they failed to renew it when they sought California Supreme Court review.

The Court of Appeal's decision is of no interest to anyone except the parties involved in this dispute. Like all unpublished California Court of Appeal decisions, it may not be cited outside the confines of this case. *See* Cal. R. Ct. 977(a). Moreover, and because of Petitioners' procedural failings, the opinion does not even address one of the two purportedly compelling questions that Petitioners now assert.

At bottom, the petition is the latest of Petitioners' numerous maneuvers to undo the inevitable consequences of their default on a multi-million dollar commercial loan. At this point, all twelve state court jurists and the one federal judge who have examined this case have rejected Petitioners' claims. Justice O'Connor recently joined that list when she denied their application for a stay in No. 00-A286. This Court should see the matter likewise and deny the petition.

## II

## STATEMENT OF THE CASE

Respondent First Pacific Bank Limited (First Pacific) cautions the Court not to rely on Petitioners' Statement of the Case. (Petn. at 2-7) That is because Petitioners have omitted from it crucial facts as well as their own procedural failings that effectively doom their request for review. For example, while the Court of Appeal's holding was based on the premise that their claim of arbitrability was "wholly groundless," in their petition, Petitioners never explain the nature of the dispute they believe should have been arbitrated. Presumably, they have omitted that explanation because it would show that the state courts correctly rejected their argument. First Pacific therefore asks the Court to look to the state Court of Appeal's recitation of the facts and procedural history [P-App. A at 1-4][1] and the other of-record documents in the

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[1] We refer to Petitioners' Appendix as "P-App." and Respondent's Appendix as "R-App."

parties' appendices – matters that First Pacific summarizes below.

In 1989 and 1991, First Pacific issued a multi-million dollar commercial loan to Petitioners Benedicto Yujuico, Teresita Yujuico and the BVY Group, Inc. (P-App. A at 1-2) The loan was secured by real property in Atherton, California that Petitioners then owned. (*Id.*) After Petitioners defaulted on their payments, First Pacific filed a foreclosure action against them. (P-App. A at 2) Rather than pay the money they owed, Petitioners forced First Pacific to litigate its right to foreclosure. Finally, in August 1997, the parties entered into a settlement ("the Agreement") that restructured the terms of the loan. (*Id.*)

Under the Agreement, and in exchange for First Pacific's agreement to reduce Petitioners' debt by several million dollars to $5.2 million, Petitioners agreed to a new payment schedule. (*Id.*) The Agreement did not provide for nor discuss payment by third parties. (*Id.* at 1)

Attached to and made part of the Agreement were: (1) a stipulated Arbitral Award ("Award") that set Petitioners' liability to First Pacific at $7.5 million; (2) a Stipulation for Enforcement of the Award, and (3) a Stipulated Judgment against Petitioners ("Stipulation") with an attached Judgment of Foreclosure and Order of Sale ("Judgment"). (P-App. A at 2) The Award allowed for foreclosure on the Atherton property and stated that, in the event of any ensuing defaults in the payments, Petitioners waived several rights pertaining to the property, including the right to redeem it after foreclosure. (P-App. A at 2, B at 3)

As the Agreement showed on its face, the key consideration for First Pacific's substantial reduction in Petitioners' debt was Petitioners' promise that there would be no more delays in paying it off. Thus, the Agreement provided that if Petitioners failed to make a payment, First Pacific would be entitled to enforce the Award and obtain the Stipulated Judgment. (P-App. A at 2) First Pacific could avail itself of these remedies without notice to Petitioners. (*Id.*)

The Agreement also provided for arbitration of any dispute "relating to or arising out of [the] Agreement" through arbitration in San Francisco, under the authority of J.A.M.S./ENDISPUTE (a California-based alternative dispute resolution organization), "in accordance with the International Arbitration Rules of the American Arbitration Association." (*Id.* at 2) Article 15.1 of those rules states that "the tribunal shall have the power to rule on its own jurisdiction, including any objection to the existence, scope or validity of the arbitration agreement."

In February 1998, First Pacific agreed to an amendment that gave Petitioners an extended payment schedule. (P-App. A at 2)[2] They then made some of the required payments. However, on September 9, 1998, petitioner Benedicto Yujuico's father, Jesus Yujuico – who was not a party to the Agreement – offered to purchase First Pacific's right to payment of Petitioners' indebtedness ("the BVY Note") on an extended payment plan and

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[2] Jesus Yujuico, petitioner Benedicto Yujuico's father, signed a guarantee that was attached to the amendment. (P-App. A at 2) However, Jesus Yujuico was only a guarantor, not a party to the amendment or to the amended Agreement. (*Id.*)

under terms that the Agreement did not include. (P-App. A at 3)

This purchase offer was *not* a tender of performance of Petitioners' obligations under the Agreement, but an offer for a new agreement with new terms and new parties. Indeed, Jesus Yujuico's representative recognized in making the proposal that "[w]e realize that you can deny our request and instead foreclose the BVY Group collateral." (P-App. A at 3)

This "realization" represented a concession that would become significant in the proceedings that later arose: nothing in the Agreement or the amendment required First Pacific to accept a substitute debtor, to agree to sale of the BVY Note, or to accept altered payment terms – and Jesus Yujuico's purchase offer would have required all three. (P-App. A at 2-3) Furthermore, First Pacific did not particularly want to become involved with Jesus Yujuico and assume the risk that he might not abide by the proposed payment plan because he had previously been involved in litigation with First Pacific, arising out of loans to a corporation in which he had been the owner. (*Id.*)

Thus, on September 10, 1998 (five days before the due date for Petitioners' next payment), First Pacific advised Jesus Yujuico that it was rejecting his proposal. (*Id.*) September 15 then came and went without Petitioners making their required $450,000 payment. On September 16, First Pacific wrote Petitioners, advising them that it would invoke its rights under the Agreement. Petitioners still did not make the payment. Instead, Jesus Yujuico reiterated his offer to substitute a new contract on

altered terms. On September 17, First Pacific again rejected his offer. (P-App. A at 3-4)

On September 30, First Pacific again wrote Petitioners, stating it would invoke its right to perfect the Stipulated Judgment under the Agreement if it did not receive payment by October 5. (P-App. A at 4) Instead of making the payment, Petitioners demanded arbitration, alleging that they had "tendered" performance by submitting Jesus Yujuico's new purchase offer. (*Id.*) First Pacific then informed Petitioners that there was no basis for arbitration – after all, the offer did not give rise to a dispute that "related to or arose out of the Agreement" – and that it would seek the remedies that the Agreement permitted. (*Id.*)

On October 9, First Pacific filed an ex parte application for enforcement of the Award and entry of the Judgment in the San Mateo County Superior Court. (P-App. A at 4) Even though Petitioners had waived their right to notice in the Agreement, First Pacific gave them notice, and they appeared at the ex parte hearing to oppose entry of the Judgment. (*Id.* at 2, 4, 6) After determining that nothing in the Agreement obligated First Pacific to accept a third party offer of substitute performance, the trial court entered the judgment of foreclosure for First Pacific, as the Agreement permitted. (*Id.* at 4)

Thirty days later, Petitioners moved to vacate the judgment. After First Pacific filed opposition and Petitioners filed a reply, and after Petitioners failed to appear at a hearing at which they had the right to contest the court's "tentative ruling," the trial court denied Petitioners' motion. (*Id.* at 4; R-App. I) In none of Petitioners'

pleadings did they mention the Federal Arbitration Act [9 U.S.C. § 2 (FAA)], much less argue that the FAA governed the alleged "dispute" over arbitrability. (R-App. II-III)[3]

Petitioners then appealed the foreclosure judgment to the California Court of Appeal. In that appeal, they made the following arguments, all based on state law: (1) First Pacific's failure to comply with the arbitration provision of the Agreement deprived it of standing to seek entry of the stipulated judgment, and the arbitration provision deprived the trial court of jurisdiction to hear First Pacific's application for entry of judgment; (2) under state contract law, First Pacific could not seek the remedies under the Agreement because it had breached the Agreement by failing to consent to the arbitration; and (3) Petitioners were denied due process. (R-App. IV) Nowhere in any of their submissions did they mention the FAA or make any argument that the trial court had erred by failing to consider federal arbitration law. (*Id.*)

On June 15, 2000,[4] the Court of Appeal affirmed the foreclosure judgment in an unpublished opinion. (P-App. A) It held that even when parties have agreed to arbitrate and to let the arbitrator determine her jurisdiction, a trial court has the right to perform a limited "gatekeeping" function and refuse to send a matter to arbitration when

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[3] First Pacific has attached to this Brief the tables of contents and tables of authorities from Petitioners' various pleadings in the state trial court, Court of Appeal and Supreme Court (and in one instance, the entire pleading because it lacks tables) to demonstrate the procedural failings that First Pacific discusses in the text.

[4] All subsequent dates are in 2000.

the court determines that a party's claim of arbitrability is "wholly groundless." (P-App. A at 5, *citing McCarroll v. L.A. County etc. Carpenters*, 49 Cal. 2d 45 (1957), *abrogated on another point Drake Bakeries v. Bakery Workers*, 370 U.S. 254, 257 (1962)). In this case, the Court held, the parties' agreement to arbitrate disputes arising out of the Agreement did not even arguably contemplate arbitration of the "dispute" relating to Jesus Yujuico's offer to substitute his own renegotiated deal for Petitioners' performance. (P-App. A at 5-6) Accordingly, because Petitioners' claim of arbitrability was wholly groundless, the Court held that the trial court properly declined to refer the matter to arbitration and that the trial court had jurisdiction to enter judgment. (*Id.*)

The Court of Appeal also rejected Petitioners' due process claim. It held that Petitioners had waived their due process rights by agreeing to the stipulated judgment and that in any event, they had received notice and had been given an opportunity to 'fully present their arguments at [the] hearing [on the entry-of-judgment proceeding] and in their motion to vacate the judgment." (*Id.* at 6) Thus, the Court held, Petitioners "received more process than they agreed to accept." (*Id.* at 7)

On June 22, Petitioners filed a petition and request for stay pending further review in the Court of Appeal. (Cal. Ct. App. No. A091568)[5] In that request, Petitioners

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[5] The stay proceedings were the consequence of Petitioners' refusal to post a bond that would have entitled them to a stay of the foreclosure judgment pending appeal. That refusal, combined with Petitioners' refusal to vacate the premises, prompted First Pacific to file an unlawful detainer

claimed, for the first time, that the Court of Appeal's reliance on *McCarroll* conflicted with this Court's decisions. On July 12, the Court of Appeal denied that petition and dissolved a 30-day stay that it had issued before oral argument.

On July 19, Petitioners filed a petition for review (Cal. Supr. Ct. No. S089988), asking the California Supreme Court to stay the unlawful detainer judgment until they had exhausted all appeals from the foreclosure judgment. The next day, Petitioners filed a petition for review of the Court of Appeal's decision in the foreclosure appeal. (Cal. Supr. Ct. No. S090027) In neither of these petitions did Petitioners assert that the trial court's proceedings had denied them due process. (R-App. V-VI) On July 24, the state Supreme Court denied both petitions. Nevertheless, First Pacific could not obtain possession of the premises because the superior court had granted a further (and final) stay of the eviction to September 23.

On September 20 – and with the final stay set to expire – Petitioners served First Pacific with a new complaint they had filed on September 14 in the Northern District of California. (*Yujuico, et al. v. First Pacific Bank Ltd.*, No. C 00-3349 PJH (N.D. Cal.)) In that lawsuit, they

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action in state court. Petitioners removed that action to the Northern District of California, but United States District Judge Saundra Brown Armstrong remanded it to state court. First Pacific then prevailed in the action and obtained a judgment of unlawful detainer. Petitioners then sought seriatim stays throughout the state court system, arguing they "needed time to pack" or other grounds that would not require them to post the bond that they previously had eschewed.

sought to rescind the Agreement on the ground that they had made a mistake of law as to First Pacific's duty to arbitrate sham arbitration demands. They predicated jurisdiction on diversity of citizenship (both First Pacific and Petitioners are foreign residents) and on alleged federal questions arising under the FAA, and sought a temporary restraining order and preliminary injunction that would stay the impending eviction and enjoin a sale of the Atherton property during the pendency of the lawsuit.

On September 22, United States District Judge Phyllis Hamilton heard the matter and denied the request for injunctive relief on the ground that petitioners had "no chance of success on the merits" because (1) their claim could have been brought in the state court litigation, (2) their alleged mistake of law was not reasonable, (3) the court refused to "intermeddle in state court proceedings out of a concern for comity," and (4) Petitioners' lawsuit "may be barred" under *Rooker v. Fidelity Trust Co.*, 263 U.S. 413 (1923), and *Dist. of Columbia Ct. of Appeals v. Feldman*, 460 U.S. 462 (1983). Judge Hamilton also encouraged First Pacific to move to dismiss the lawsuit. Petitioners agreed at the September 22 hearing to voluntarily dismiss, however, and did so on September 27.

On September 28, Petitioners filed a petition for a stay of the foreclosure judgment pending certiorari in the state Court of Appeal. On October 2, the Court of Appeal denied the petition. The following day, Petitioners filed in this Court an application to stay the "mandate" [*sic*] of the California Court of Appeal. Although they had just argued to Judge Hamilton that *they* had mistakenly construed the effect of the arbitration clause, they told this

Court that the *state courts* had mistakenly applied federal arbitration law. (Application For Stay of Mandate, No. 00-A286) Justice O'Connor denied the application on October 3. The eviction went forward as scheduled on that day.

Petitioners now seek certiorari, presenting the same arguments that they made in their stay application to Justice O'Connor.

## III

## REASONS THE PETITION SHOULD BE DENIED

Petitioners assert as worthy of certiorari one issue they did not raise until after the California Court of Appeal affirmed the foreclosure judgment and a second issue that they failed to present to the California Supreme Court. The first issue is whether state courts have the right, without running afoul of the FAA, to perform a "gatekeeping" function and to decline to refer to an arbitrator wholly groundless arbitrability claims. The second issue is whether the state court's entry of the stipulated judgment after an ex parte proceeding (in which Petitioners participated) and a motion to vacate proceeding (which Petitioners initiated) denied Petitioners due process under the Fourteenth Amendment.

Neither of these issues presents a "compelling" or "important" question – the criteria for review under this Court's rules. S. Ct. R. 10. The unpublished Court of Appeal decision here has no effect on future cases or the development of the law and may not be cited outside the confines of this case. *See* Cal. R. Ct. 977(a). Moreover, both claims that Petitioners raise are not subject to

serious debate, and Petitioners failed to properly press either in the state courts.

### A. Petitioners' Failure To Raise In A Timely And Proper Way In The State Courts The Issues They Are Raising In Their Petition Is Reason Alone For The Court To Deny Certiorari

As a matter of comity, this Court will not review a state court judgment unless the party seeking review brought its federal claim "to the attention of the state court with fair precision and in due time." *New York ex rel. Bryant v. Zimmerman*, 278 U.S. 63, 67 (1928). Although one may debate what constitutes "fair precision and in due time," "[a]t the minimum there should be no doubt from the record that a claim under a federal statute or the Federal Constitution was presented in the state courts and that those courts were apprised of the nature or substance of the federal claim at the time and in the manner required by the state law." *Webb v. Webb*, 451 U.S. 493, 501 (1981).

Petitioners failed in several ways to present their present claims "at the time and in the manner required by the state law." *Id.* They did not raise the first claim – an alleged violation of federal arbitration law – in the trial court or in their appeal to the state Court of Appeal until after the Court of Appeal filed its opinion. Each of these failings violated separate state procedural rules. *See Hughes v. Blue Cross of N. Cal.*, 215 Cal. App. 3d 832, 849-53 (1989) (failure to raise claim of federal preemption in state trial court precludes review of preemption issue on appeal); *People v. Scott*, 14 Cal. 4th 544, 553 (1996)

(failure to raise issue in state court of appeal normally bars further review of issue by state supreme court); Cal. R. Ct. 29(b)(1) (same) They also did not raise their second claim – an alleged violation of due process – in the California Supreme Court when they sought review of the Court of Appeal's decision.

As a consequence of Petitioners' failings, no discussion of their first issue appears anywhere in the Court of Appeal opinion that they challenge, and the highest state court was never given an opportunity to rule on their second issue.

Even when this Court *grants* certiorari, it will decline to review issues that the litigants did not fairly present to the state courts. *See Clark v. Jeter*, 486 U.S. 456, 459 (1988) (declining to consider whether federal Child Support Enforcement Amendments preempted state court interpretation of state statute of limitations where litigant failed to adequately present federal question to state courts); *Bankers Life and Casualty Co. v. Crenshaw*, 486 U.S. 71, 77-78 (1988) (declining to consider federal due process claim where petitioner first raised due process issue in petition for rehearing in state supreme court but, even then, did not specify that claim was grounded in federal as well as state constitution); *Webb*, 451 U.S. at 495 (declining to review issue where "nowhere in the opinion of the Georgia Supreme Court is any federal question mentioned, let alone expressly passed upon. Nor is any federal issue mentioned by the dissenting opinion in that court.").

If the failure to properly press a federal issue in the state courts precludes review in those few cases in which

this Court *grants* certiorari, surely petitioners' failure to properly raise their present claims dooms their *request* for certiorari. Indeed, Petitioners do not even attempt to explain these failings – as this Court's rules require – because they cannot. *See* S. Ct. R. 14.1(g)(i) (requiring litigants who seek review of a state court judgment to specify "the stage in the proceedings, both in the court of first instance and in the appellate courts, when the federal questions sought to be reviewed were raised; the method or manner of raising them and the way in which they were passed on by those courts"). The Court should therefore deny the petition for these reasons alone.

### B. In Any Event, Neither Of The Issues Petitioners Raise Warrants This Court's Attention

Procedural defects aside, there is no valid reason on the merits for granting certiorari on either of the issues Petitioners have raised. Neither qualifies for certiorari review, and on neither did the state courts err.

#### 1. There Is No Conflict Between The California Supreme Court's *McCarroll* Decision And This Court's Precedents Concerning Arbitral Jurisdiction

This Court consistently has held that the FAA requires a court to apply ordinary contract law to determine whether parties to a contract (1) intended to submit a given dispute to arbitration, and (2) intended that the arbitrator rather than the court would determine the arbitrability of that dispute. *See, e.g., First Options of Chicago v. Kaplan*, 514 U.S. 938, 943 (1995) ("arbitration is simply a

matter of contract between the parties; it is a way to resolve those disputes – but only those disputes – that the parties have agreed to submit to arbitration.").

For almost half a century, the California Supreme Court has adhered to this rule. In *McCarroll v. L.A. County etc. Carpenters*, 49 Cal. 2d 45, the California Supreme Court held: "The arbitrability of a dispute may itself be subject to arbitration if the parties have so provided in their contract. In this situation, the court should stay proceedings pending the arbiter's determination of his own jurisdiction *unless it is clear that the claim of arbitrability is wholly groundless.*" *Id.* at 65 (emph. added).

This holding represents nothing more than an application of the established principle that a court should interpret a contract in a manner that renders it "reasonable and capable of being carried into effect" [Cal. Civ. Code § 1643] and that avoids absurd results [Cal. Civ. Code § 1638]. Thus, if parties to a contract have agreed to let an arbitrator determine her jurisdiction over a dispute, the court must stay proceedings pending the arbitrator's determination of that threshold arbitrability issue. But if the claim of arbitrability is "wholly groundless," the court has the power to intervene to protect the legitimate expectations of the party who never agreed that such a sham claim would be referred to an arbitrator. *See McCarroll*, 49 Cal. 2d at 66 (whether court rather than arbitrator should make the jurisdictional call in the first instance must "reflect the intention of the parties"), 68-69 (principle favoring expansive construction of arbitration provisions "does not justify overriding the parties' intentions and forcing on them a method of decision wholly unexpected in its application").

*McCarroll* is in accord with federal arbitration law. Under the analogous arbitration provisions of the federal Labor Management Relations Act, one federal court has enunciated the same gatekeeping rule that *McCarroll* articulated. *See Local No. 358 Bakery & Confec., etc. v. Nolde Bros., Inc.*, 530 F. 2d 548, 553 (4th Cir. 1975) ("[T]he arbitrability of a dispute may itself be subject to arbitration if the parties have clearly so provided in the agreement. Of course, the court must decide the threshold question whether the parties have in fact conferred this power on the arbitrator. If they have, the court should stay proceedings pending the arbitrator's determination of his own jurisdiction, *unless it is clear that the claim of arbitrability is wholly groundless.*" (Emph. added); court compelled arbitration under collective bargaining agreement).

Indeed, *McCarroll* itself based its "gatekeeping" rule on federal cases interpreting the FAA. *See McCarroll*, 49 Cal. 2d at 65 (citing *International Un., United Auto. Aircraft v. Benton Harbor Malleable Indus.*, 242 F. 2d 536, 539 (6th Cir. 1957); *Local 205, United Elec. Etc. Workers v. General Elec. Co.*, 233 F. 2d 85, 101 (1st Cir. 1957)). Thus, Petitioners are simply wrong in their claim that federal law "provides no such exception to enforcement of arbitration agreements governed by the FAA." (Petn. at 15)

*McCarroll* and its federal counterparts are garden variety applications of the FAA rule that, where the parties have agreed to submit contract interpretation questions to the arbitrator, a court's role is "confined to ascertaining whether the party seeking arbitration is making a claim which on its face is governed by the contract." *United Steelworkers v. American Mfg. Co.*, 363

U.S. 564, 568 (1960). Obviously, if it is "clear" that a claim of arbitrability is "wholly groundless," then the party seeking arbitration is *not* making a claim that on its face is governed by the contract.

*McCarroll* and its federal counterparts also mirror the federal rule that, despite a presumption of arbitrability that might attach to an arbitration agreement, a court should not order arbitration if it can say with "positive assurance" that the parties did not intend the arbitration clause to cover the parties' dispute. *See ITT Hartford Life & Annuity Ins. Co. v. Amerishare Investors, Inc.*, 133 F. 3d 664, 668-70 (8th Cir. 1998) (holding "with positive assurance" that arbitration clause in marketing agreement did not cover action to collect on loan guarantees); *see also Wright v. Universal Maritime Servs. Corp.*, 525 U.S. 70, 78 (1998) (court's "positive assurance" that parties did not intend to arbitrate dispute overcomes presumption of arbitrability that otherwise would attach under the Labor Management Relations Act).

Both the "gate-keeping" rule that *McCarroll* recognized and its identical federal counterpart, together with the rules that courts apply under the FAA, follow logically from the FAA's fundamental command – that the parties' intentions control their obligations to arbitrate and to present an arbitrability claim to an arbitrator in the first instance. *McCarroll* follows that command because, as explained, it seeks strictly to enforce the parties' intentions.

This case demonstrates that a court must retain a limited gatekeeping function to determine if a claim of

arbitrability is "wholly groundless." As the Court of Appeal stated:

> Under [Petitioners'] theory, they could fail to make a payment and file an arbitration demand, alleging that payment was excused because the sky was gray on the payment date. They could then successfully argue that [First Pacific] was in breach by seeking entry of the [stipulated judgment] on the ground that their 'gray sky' 'excuse' for nonpayment gave rise to a dispute that 'arose out of' the [arbitration agreement] and had to be arbitrated, and that only an arbitrator could determine arbitrability. [¶] Once that sham claim of arbitrability was resolved, [Petitioners] could manufacture yet another purportedly arbitrable dispute – claiming for example, that payment was not due because the sun set before 7 p.m. on the payment date. (Opin. at 5-6, *quoting* First Pacific's Respondent's Brief (some brackets in orig.))

Petitioners have never challenged this reasoning. Small wonder, because it is unassailable. Indeed, although the parties here agreed to a broad arbitration clause and to permit an arbitrator to determine arbitrability, they did not reasonably intend to arbitrate everything under the sun or to permit an arbitrator to determine the arbitrability of *any* conceivable dispute. Because courts reject any contract interpretation that produces absurdities – whether or not the contract involves arbitration – the arbitration clause here necessarily permitted a court to exercise a limited gatekeeping power to reject a sham arbitrability demand.

This Court need not grant certiorari to revisit this conclusion because it is self-evident. All courts adhere to

the rule that underlies it, as shown by the unbroken line of decisions by the fourteen jurists who have examined this case.

Because they cannot show any conflict between state and federal law, petitioners instead misstate *McCarroll*'s holding: "The *McCarroll* decision permits judicial consideration of the merits of a dispute governed by the FAA *before* submitting the matter to arbitration if the superior court determines that the claim is 'wholly groundless.' " (Petn. at 3-4, emph. in orig.)

*McCarroll* does no such thing. When the parties have agreed to permit an arbitrator to determine the arbitrability of disputes arising out of the parties' agreement, *McCarroll* requires a court to submit the claim to arbitration "unless it is *clear* that the *claim of arbitrability* is wholly groundless." 49 Cal. 2d at 65 (emph. added). This is the barest minimum of judicial scrutiny. It permits a court to refuse an arbitrability demand that is a clear sham; it does not permit a court to pass on the merits of the dispute. Indeed, if the court did not retain this minimal gatekeeping power, contracting parties would be powerless to resist a potentially endless series of sham arbitration demands, as the state Court of Appeal here observed. Because Petitioners and First Pacific could not have intended that result, the state courts were correct in relying on *McCarroll* and in refusing to refer this case to arbitration.

To further their invention of a conflict between federal and state law, Petitioners state that *McCarroll* recognized that it was "in 'irreconcilable conflict' with some of the federal decisions at that time. (*McCarroll, supra,* 49

Cal. 2d at 67.)" (Petn. at 5-6) But the "conflict" to which *McCarroll* was referring related to whether a standard collective bargaining agreement requires arbitration – not whether courts may perform a limited gatekeeping role in weeding out sham arbitrability claims. *See* 49 Cal. 2d at 67. As explained, *no* case conflicts with *McCarroll* on the principle at issue here – when parties agree to let an arbitrator determine her jurisdiction over disputes "arising out of the agreement," a court retains a limited gatekeeping function to determine whether an arbitration demand is "wholly groundless."

Having mischaracterized *McCarroll*, Petitioners then draw analogies between it and state laws that this Court has struck down under the FAA. *See Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 280-81 (1995) (state statute invalidated all pre-dispute arbitration agreements); *Perry v. Thomas*, 482 U.S. 483, 489-91 (1987) (state statute permitted wage collection action without regard for any private arbitration agreement); *Southland Corp. v. Keating*, 465 U.S. 1, 10-16 (1984) (state statute voided any contract that required franchisee to arbitrate).

But the reason why the statutes at issue in these cases violated the FAA was that they attempted to treat arbitration agreements differently from other contracts, thereby potentially defeating the legitimate expectations of parties to an arbitration agreement. Here, however, *McCarroll*, like the federal cases that are consistent with it, applies ordinary contract law principles to *protect* the parties' legitimate expectations. *McCarroll* thus directs

courts to treat arbitration agreements like any other contract. This is precisely what the FAA requires.[6]

Petitioners also argue that *McCarroll* should be limited to its facts. But nothing in *McCarroll* indicates that its gatekeeping rule should be limited to the context in which *McCarroll* arose. The issue in *McCarroll* was whether contractors who were parties to a collective bargaining agreement ("CBA") with certain labor unions were prohibited from maintaining a lawsuit against the unions for unlawful strikes that the unions had allegedly called, on the ground that the dispute was arbitrable under the CBA. The unions argued that under the CBA, only an arbitrator could determine the arbitrability of the contractors' claim that the unions had violated the CBA's no-strike clause. 49 Cal. 2d at 65-66.

The California Supreme Court held that the trial court properly concluded that the parties did not contemplate arbitration of a breach of the no-strike clause, even though the arbitration clause broadly required arbitration of " 'all grievances or disputes arising between . . . [the parties] over the interpretation or application of the terms of this Agreement. . . . ' " *Id.* at 67. The Court noted that the arbitration clause was contained in "Article V" of the CBA, which was designed to deal with employee complaints concerning "working conditions, wrongful

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[6] *McCarroll* is therefore consistent with the recent Ninth Circuit decision that Petitioners cite. *Portland Gen. Electric Co. v. U.S. Bank Trust Nat. Assoc.*, 218 F. 3d 1085, 1090 (9th Cir. 2000) (because parties' appraisal agreement specified that Oregon law would govern contract, Oregon law, not FAA, governed agreement).

discharge, and the like," and that it was "inconceivable that the parties thought an employer would be required to follow these steps [preliminary complaint to a craft steward, adjudication by a 'special representative,' and eventually arbitration] in prosecuting his objection to a strike." *Id.* at 67-68. Even more persuasive, the Court found, was that the grievance and arbitration procedure was an *alternative* to a strike as the means to settle disputes, "and it is clear that the parties bound themselves to resort to [the grievance] procedure for the very purpose of avoiding the possibility of a strike . . . not to adjudicate a strike once it has occurred. . . . " *Id.* at 68.

What is significant from this discussion is not so much the details and the operation of the particular arbitration provision in *McCarroll*, but that the California Supreme Court found it appropriate to analyze that provision and determine whether the parties' dispute fit within its terms. The Court emphasized that the determination of whether a court rather than an arbitrator should make the jurisdictional call in the first instance was one that needed to "reflect the intention of the parties." *Id.* at 66. And, the Court noted, although courts should construe arbitration provisions in collective bargaining agreements broadly, that principle "does not justify overriding the parties' intentions and forcing on them a method of decision wholly unexpected in its application." *Id.* at 68-69.

This is First Pacific's precise point. Nothing in the Agreement indicates the parties intended to submit a "wholly groundless" "dispute" about a third party's purchase offer to an arbitration between First Pacific and Petitioners, or to permit an arbitrator to determine whether First Pacific's rejection of such a third party offer

would be arbitrable. And nothing in *McCarroll* suggests that its holding concerning judicial responsibility to weed out sham arbitrability demands was limited to the collective bargaining context.[7]

Petitioners correctly note that commercial arbitration agreements that the FAA governs have assumed greater importance in modern life. But that truism provides no basis for reviewing the mundane questions in their petition, on which there is no serious debate in the state and federal courts and which petitioners did not even properly raise below.

**2. Even Though They Waived Their Due Process Rights, The Trial Court Gave Petitioners Full Due Process In Connection With Entry Of The Judgment, So There Is No Basis For Their Due Process Claim**

Litigants may waive their right to due process by a contract that stipulates to the entry of judgment by expedited process. *See D.H. Overmyer Co. v. Frick Co.*, 405 U.S.

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[7] This Court later abrogated that portion of *McCarroll*'s holding that decided that a standard collective bargaining agreement does not require arbitration. *See Drake Bakeries v. Bakery Workers*, 370 U.S. 254, 257-59 (1962). But nothing in *Drake Bakeries* undermines that portion of *McCarroll*'s holding on which *this* case turns – that when parties agree to let an arbitrator determine her jurisdiction over disputes "arising out of the agreement," a court retains a limited gatekeeping function to determine whether an arbitrability demand is "wholly groundless." Thus, as the state Court of Appeal recognized, *Drake Bakeries* does not affect the application of the relevant *McCarroll* principle here. (P-App. A at 6 n.3) Petitioners' suggestion to the contrary is wrong. (*See* Petn. at 6)

174, 187 (1972) (debtor waived right to notice and hearing before deprivation of property when, while represented by counsel, debtor signed a document that authorized judgment by confession); *FRG, Inc. v. Manley*, 919 F. 2d 850, 857 (3d Cir. 1990) (party waived due process rights where "the confession of judgment clause here was negotiated and specifically agreed upon in a commercial context in settlement of major litigation between parties represented by counsel").

Consistent with these principles, California law authorizes such due process waivers in order to permit the prompt and efficient resolution of litigation. *See Rooney v. Inv. Co.*, 10 Cal. 3d 351, 358 (1973) ("When a written stipulation sets forth all the terms of a judgment agreed to by the parties, the filing of the stipulation normally provides sufficient basis for entry of judgment upon the ex parte application of either party."). This common sense rule easily satisfies the Fourteenth Amendment because it simply enforces a litigant's bargained for stipulation to expedited process.

Here, while represented by counsel and after lengthy negotiations, Petitioners agreed that if they breached the Agreement, First Pacific could obtain entry of the Judgment "without further notice" to Petitioners. (P-App. A at 2, 6) That waiver was part of the consideration for First Pacific's agreement to shave millions of dollars off of Petitioners' debt and to give them yet another chance to make good on their loan obligations. Because Petitioners voluntarily and intelligently waived their due process rights for valuable consideration, the state trial court constitutionally could have entered judgment without

affording petitioners notice and an opportunity to be heard.

But the state trial court *did* afford petitioners that notice and opportunity. They received notice of the setting of the ex parte hearing on the entry of judgment and appeared on the day the hearing was set. They also presented written opposition to the trial judge and conveyed oral argument through the judge's research attorney. (P-App. A at 4, 6) And, although no more was required, they then filed and set a hearing on a motion to vacate the judgment. The hearing would have occurred but for *Petitioners'* decision not to contest the court's tentative ruling, which was against them. (*Id.*; R-App. I) Each of these procedures gave Petitioners ample opportunity to raise any arguments in opposition to entry of the judgment of foreclosure. *See In re Marriage of Jacobs*, 128 Cal. App. 3d 273, 285-86 (1982) (under California law stipulated judgment will be set aside if moving party demonstrates grounds for vacating the judgment). Considering that Petitioners expressly waived their due process rights, the notice and opportunity to be heard that they received easily satisfied the Fourteenth Amendment.

Petitioners have not cited a single case that found a due process violation on even remotely analogous facts, much less demonstrated a substantial conflict or confusion in the lower courts on this issue. Their due process claim is so flimsy that even they omitted it from their petition for review in the California Supreme Court. This Court need not grant certiorari to review a claim that even the petitioners did not think worthy of a state high court's review.

## IV

## CONCLUSION

Petitioners are raising claims here that they did not properly present to the state courts below. Their current claims neither address nor involve any substantial questions of law, and the state Court of Appeal's decision has no precedential value. The parties and the system already have invested far more resources examining this matter than this case merits. This Court should therefore deny the petition for a writ of certiorari.

Dated: November 9, 2000.

Respectfully submitted,

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## APPENDIX I

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First Pacific Bank Limited,
a Hong Kong banking corporation

SUPERIOR COURT OF CALIFORNIA –
COUNTY OF SAN MATEO

FIRST PACIFIC BANK LIMITED, a Hong Kong banking corporation,

Plaintiff,

vs.

THE BVY GROUP, a California Corporation, et al.,

Defendants.

_____/

THE BVY GROUP, a California corporation, et al.,

Cross-Complainants,

vs.

FIRST PACIFIC BANK LIMITED, a Hong Kong banking corporation, et al.,

Cross-Defendants.

_____/

No. 391951

ORDER DENYING DEFENDANTS' THE BVY GROUP, INC., BENEDICTO V. YUJUICO AND TERESITA YUJUICO'S MOTION TO VACATE JUDGMENT

Date:
December 3, 1998
Time: 9:00 a.m.
Dept.:
Law & Motion;
Dept. 10

(Filed Dec. 8, 1998)

Defendants' motion to vacate judgment was set for hearing in Department 10 of the above-entitled court before the Honorable Judith Whitmer Kozloski, on December 3, 1998. The Court, having considered the pleadings and all documents filed relating to defendants' motion, and good cause appearing, issued its tentative ruling on December 2, 1998 pursuant to San Mateo County Superior Court Local Rule 3.5, denying defendants' motion to vacate the judgment. There having been no appearance by counsel for the parties to contest the tentative ruling, IT IS HEREBY ORDERED that:

Defendants' motion to vacate judgment is denied.

DATED: December 8, 1998

By Judith Whitmer Kozloski
Honorable Judith Whitmer Kozloski
Judge of the Superior Court

## APPENDIX II

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Benedicto V. Yujuico and Teresa Yujuico

**SUPERIOR COURT OF THE STATE OF CALIFORNIA
IN AND FOR THE COUNTY OF SAN MATEO**

| | |
|---|---|
| FIRST PACIFIC BANK LIMITED, a Hong King banking corporation,<br><br>First Pacific,<br><br>v.<br><br>THE BVY GROUP, a California corporation; et al.,<br><br>Defendants. | Case No. 391951<br><br>**MEMORANDUM OF POINTS AND AUTHORITIES IN OPPOSITION TO EX PARTE APPLICATION FOR ENFORCEMENT OF ARBITRATION AWARD AND ENTRY OF STIPULATED JUDGMENT** |
| AND RELATED CROSS-ACTIONS. | Date: October 9, 1998<br>TIME: 2:00 p.m.<br>DEPT: 10 |

Defendants and Cross-Complainants the BVY Group, Benedicto V. Yujuico and Teresita Yujuico (collectively, "BVY") hereby respectfully submit the following Memorandum of Points and Authorities in Opposition to the

Ex Parte Application of First Pacific First Pacific Bank ("First Pacific") for Enforcement of Arbitration Award and Entry of Stipulated Judgment (the "Application"):

## INTRODUCTION

This court lacks jurisdiction to hear First Pacific's Application. As we show, the parties are subject to a broad and all encompassing arbitration agreement pursuant to which they agreed to submit to binding arbitration "any dispute" between them "relating to or arising out of" a settlement agreement reached in this action in August 1997. On October 2, 1998, BVY submitted to JAMS/Endispute ("JAMS"), the tribunal selected to preside over any dispute under the settlement agreement, a Demand for Arbitration seeking resolution of pending disputes concerning performance under the settlement. Thus, on that date, arbitration proceedings commenced and this Court does not, respectfully, have jurisdiction to hear this matter.

By its Application, First Pacific seeks the entry of a judgment that exceeds by $2,300,000 the agreed-upon settlement amount, following First Pacific's unreasonable and improper rejection of a timely tender of performance under the settlement agreement. As we show, this tender would have made First Pacific whole and was entirely reasonable. Thus, bona fide disputes exist as to whether BVY is in default and whether First Pacific is entitled to seek entry of judgment. These issues, together with the jurisdictional question, if any, must be decided in arbitration.

Even if the Court were to reach the substantive issues that now exist, which it should not, it must nonetheless decline to grant the requested relief. First, First Pacific is not entitled to entry of judgment because there has been no breach. BVY has already paid 65% of the amount owing and has tendered to First Pacific the balance on terms that actually *improve* the position of First Pacific. This tender constitutes substantial performance under applicable law and prevents a finding of default. What is more, even if this Court had jurisdiction and even if BVY had breached the Agreement, the difference between the $5,200,000.00 agreed-to and the $7,500,000.00 value of the proposed judgment constitutes an unenforceable forfeiture and a penalty. The circumstances giving rise to the present dispute provide a compelling case for application of the equitable and statutory principles that preclude forfeiture of real property and the imposition of penalties.

First Pacific's Application is nothing more than an improper attempt to circumvent the clear terms of the arbitration agreement and to obtain an improper forfeiture. Accordingly, BVY respectfully submits that this Application must be summarily denied.

## II. STATEMENT OF FACTS

### A. The Underlying Settlement And Arbitration Agreements

On or about August 1, 1997, BVY Group, Benedicto V. Yujuico and Teresita Yujuico (collectively, "BVY") and First Pacific entered into an Agreement of Compromise and Settlement, Release, and Covenant Not To Sue (the

"Agreement"), in settlement of this litigation. Pursuant to the Agreement, BVY agreed to pay First Pacific the total sum of $5.2 million in three installments of $3 million, $1.1 million and $1.1 million on August 29, 1997, January 15, 1998 and August 15, 1998, respectively. A residence belonging to defendants and cross-complainants Benedicto and Teresita Yujuico in Atherton, California, secured these payment obligations ("the Property"). Declaration of Benedicto V. Yujuico ("Yujuico Decl.") ¶ 3.[1] The Agreement further provides that if BVY commits a payment default, First Pacific may submit a request to the Court to enter a Stipulation for Enforcement of Arbitration Award and Stipulated Judgment in the increased amount of $7,500,000.00 and may seek to foreclose nonjudicially on the Property. Yujuico Decl., Exh. A.

In negotiating the Agreement, First Pacific insisted that any disputes that might arise in connection with the Agreement be submitted to arbitration. Coffino Decl. ¶ 3. First Pacific also insisted that the arbitration be controlled by the International Arbitration Rules of the American Arbitration Association. Coffino Decl. ¶ 3. Accordingly, First Pacific, who drafted the settlement documentation, included in the Agreement an exclusive and all-encompassing arbitration clause. Coffino Decl. ¶ 3. Specifically, the Agreement provides as follows: **"In the event of any dispute relating to or arising out of [the] Agreement, the**

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[1] The Yujuico Declaration is attached to the Declaration of Michael J. Coffino ("Coffino Decl.") as Exhibit 1 and is in facsimile form. Because First Pacific has elected to proceed on an ex parte basis and Mr. Yujuico is in the Philippines, we had no choice but to obtain a facsimile declaration.

**exclusive forum for resolution of any such dispute shall be by arbitration in San Francisco, California under the authority of JAMS/Endispute in accordance with the International Arbitration rules of the American Arbitration Association** (the "Arbitration Rules"). Yujuico Decl., Exh. A ¶ 19.

**B. Performance by BVY Under the Agreement**

In accordance with the Agreement, BVY timely made the initial $3 million payment to First Pacific. Subsequently, the entire Asian continent became plagued by one of worst economic crises in our time. In the third quarter of 1997, for example, the exchange rate for the Philippine peso was P26 to US$1.00; today, the rate is approximately P44 to US$1.00. Yujuico Decl. ¶ 2. In January 1998, in light of difficult economic circumstances, BVY negotiated a restructuring with First Pacific in the form of an amendment to the Agreement ("the Amendment"). Under the Amendment, First Pacific increased the interest rate to 9.5% (from 7%) and altered the payment schedule. The Amendment states that several payments totaling $450,000 would be paid over the course of several months in different amounts. The next $450,000 would be due on September 15, 1998; the next $650,000 on March 15, 1999; and the final $650,000 on September 15, 1999. Yujuico Decl., Exh. B.

Despite very difficult economic circumstances, BVY made the six payments called for between February and August 1998 pursuant to the Amendment. BVY would always advise First Pacific in advance of any difficulty anticipated in meeting a strict due date and invariably

First Pacific would consent to an extension of the due date. As detailed in prior declarations in the underlying litigation that culminated in the Agreement, First Pacific and BVY have had a very unique relationship, which has included, among other things, stock ownership by First Pacific Bank in BVY and a long history of restructures and oral and informal agreements. Yujuico Decl. ¶ 7. To date, BVY has paid $3,450,000 and has tendered the $450,000 due on September 15, 1998, which, as explained below, First Pacific declined to accept.

On September 9, 1998, due to a variety of economic circumstances, the father of Benedicto Yujuico, Jesus Yujuico, offered to *improve* the payment schedule set forth in the Amendment. He offered to pay First Pacific $450,000 on September 16, 1998 and the entire balance of $1,300,000 on March 15, 1999, even though the final $650,000 was not due until September 15, 1999. In connection with this tender, Mr. Jesus Yujuico requested that First Pacific sell him the BVY note and take a new note on the terms outlined above. He agreed that First Pacific would retain all the same collateral (including the Arbitration Award and Stipulated Judgment). He also offered to pay all of First Pacific's legal fees and $10,000 of its administrative costs in preparing necessary documentation. Yujuico Decl. ¶ 9. First Pacific rejected this tender of performance. By letter dated September 30, 1998, First Pacific demanded payment of the $450,000 due on September 15, 1998. Yujuico Decl., Exh. C. Despite the rejection of the tender, BVY remains willing to perform in accordance with the tender of performance. As a good faith gesture, BVY is also willing to put in escrow 50% of

what is due currently under the Amendment pending the outcome of the arbitration proceedings.

### C. Commencement of Arbitration

On October 2, 1998, BVY served on First Pacific and its counsel and submitted by hand delivery to JAMS, the arbitration tribunal selected by First Pacific, a Demand for Arbitration in accordance with Paragraph 19 of the Agreement. Coffino Decl. ¶ 4 & Exh. 2 (Demand). Pursuant to Article 2 of the Arbitration Rules, the submission the arbitration demand commenced arbitral proceedings. Coffino Decl., Exh. 3 (Rules). "Arbitral proceedings shall be deemed to commence on the date on which the administrator receives the notice of arbitration." *Id.*

On October 5, 1998, at the request of BVY, JAMS scheduled a hearing for October 15, 1998 to determine whether First Pacific was required to participate in the arbitration and to determine whether First Pacific should be restrained – pursuant to Article 21 of the Arbitration Rules allowing injunctive relief – from seeking Court intervention pending the outcome of the arbitration. Coffino Dec. ¶ 5. On October 7, 1998, First Pacific confirmed its willingness to appear at the hearing subject to a reservation of rights. Coffino Decl., Exh. 3. The very next day, however, First Pacific attempted to make an end-run around the arbitration agreement by notifying BVY of this Ex Parte Application.

## III. LEGAL ARGUMENT

### A. This Court Lacks Jurisdiction To Hear First Pacific's Application

Upon the commencement of arbitration proceedings, the arbitrator "takes over" and in consequence assumes exclusive jurisdiction to decide all questions needed to resolve the controversy and all issues relating to procedure and discovery. *Van Tassel v. Superior Court*, 12 Cal. 3d 624, 627 (1974); *Titan/Value Equities Group, Inc. v. The Superior Court of San Diego County*, 29 Cal.App. 4th 482, 487-88 (1994); Accordingly, once a case is submitted to arbitration, the trial court lacks jurisdiction to resolve procedural questions, order discovery or determine the status of claims before the arbitrator. *Id.* at 489.

Here, BVY commenced arbitration on October 2, 1998 in accordance with the rules selected by First Pacific. By so doing, BVY properly invoked the jurisdiction of the arbitration tribunal, also selected by First Pacific, to determine whether in fact BVY committed a default under the terms of the Agreement. This central issue is unequivocally a "dispute relating to or arising out of [the Agreement]," which falls squarely within the parties' arbitration agreement. In addition, JAMS must decide the nature of the rights and obligations under the Agreement under the present circumstances whether and, if so, to what extent, First Pacific Bank may enforce the Agreement at this time.

We anticipate that First Pacific will argue there is no arbitrable dispute worthy of arbitration. Such an argument betrays a misunderstanding of the arbitrable process and the jurisdiction of the arbitrator. It is well settled

that it is the province of the arbitrator, not that of the Court, to decide questions of his or her jurisdiction. C.C.P. §§ 1297.161-163; *McCarroll v. L.A. County Carpenters* (1957) 49 Cal.2d 45, 65-66. Not surprisingly, the Arbitration Rules expressly vest the arbitrator with the authority to decide issues of jurisdiction. Article is Exhibit "1" hereto. Indeed, in international arbitrations, challenges to the jurisdiction of the arbitrator are made *in the arbitration*. C.C.P. § 1297.162. Court involvement is expressly limited to reviewing jurisdictional decisions made *by the arbitrator* during the course of those proceedings. C.C.P. § 1297.166.

The attempt by First Pacific to embroil the Court in this process, is a breach of the arbitration clause and, if permitted, would eviscerate a provision in the Agreement that First Pacific demanded be made a material part of the compromise reached last year. Equally important, the attempt by First Pacific to ignore the arbitration clause is squarely at odds with the Arbitration Rules it insisted must govern future disputes between the parties, contravenes the provisions of code of Civil Procedure governing international arbitration and offends the spirit and sanctity of the arbitration process.

For these reasons, the Court must, we respectfully submit, deny the ex parte application submitted by First Pacific.

### B. There Are Bona Fide Disputes Subject to Arbitration

Although we believe that this court may not decide the jurisdiction of the arbitrator at this time, and thus

submit that whether or not an arbitrable dispute exists is entirely irrelevant to the Application, we now show that a bona fide dispute exists under the Agreement that must be resolved by arbitration before First Pacific may, if at all, proceed to invoke the jurisdiction of this Court.

1. BVY Have Substantially Performed Under The Agreement

Under the doctrine of substantial performance, a party who has "substantially performed" the terms of a contract may be entitled to complete performance under the agreement, rather than be subject to damages for default. Corbin, *Contracts*, §§ 700-701 (West Publishing 1982). In general, a party has substantially performed if there has been no willful departure from the terms of the contract, the party has in good faith performed all of the substantive terms of the contract, and the "defect" can be easily remedied such that the other party will get "almost" what the contract requires. *Posner v. Grunwald-Marx, Inc.*, 56 Cal. 2d 169, 187 (1961); *Bonadelle Constr. Co. v. Hernandez*, 169 Cal. App. 2d 396, 399 (1959); Corbin § 707 (the higher the ration of performance to non-performance, the more likely there has been substantial performance); *Scarbery v. Patch Land and Water Co.*, 184 Cal.App. 2d 87, 105 (1960) (payment of $150,000 of a $200,000 obligation found substantial enough to outweigh default).[2]

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[2] The doctrine is consistent with the concept of a "material breach," which is determined pursuant to the following factors: (i) the extent to which the injured party will obtain the

In determining whether a party has substantially performed, a party's good faith or, alternatively, willfulness in performing must be taken into account. *Id.* Thus, in *Commercial Discount Co. v. Town of Plainfield* 180 A. 311 (1935), a contractor who had completed approximately 90% of a construction job but who was forced to cease work due to financial difficulties was considered not to have behaved willfully or intentionally and, thus, to have substantially performed the contract.

It is plain that under applicable law whether a party has substantially performed presents a fact question for the trier of a fact. Here, there is no question that BVY have substantially performed the Agreement. Each of the payments due prior to September 15, 1998 was made in full and accepted without complaint. To date, BVY have paid a total of $3,450,000 of principal under the Agreement, which represents approximately 65% of the total principal obligation. Moreover, BVY tendered performance of the balance of the payment obligations on terms that provided First Pacific with a *better* economic package than what is in place. It only asked for an immaterial alteration of the documents which did not prejudice First

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substantial benefit of what he expected; (ii) the extent to which the injured party may be adequately compensated in damages for lack of complete performance; (iii) the extent to which the party failing to perform has already partly performed; (iv) the degree of hardship the defaulting party would suffer on termination of the contract; (v) the willfulness or innocence of the non-performing party; and (vi) the degree of certainty that the party will complete performance. *Sackett v. Spindler* (1967) 248 Cal.App.2d 220, 229.

Pacific in any way. In fact, it even offered to pay for the costs of making those minor alterations.

This performance comes in the middle of a severe repression that is undermining markets in Asia in an unprecedented and alarming manner. The circumstances surrounding the creation of the Agreement have changed dramatically. Still, BVY has at all times acted reasonably and have attempted to live up to the strict terms of the Agreement. It has acted in utmost good faith and, as a further gesture of good faith, has even offered to put a substantial sum in escrow pending the outcome of the arbitration. Yujuico Decl. ¶ 13.

The slight document alteration requested by BVY is fully consistent with the course of dealing that has existed between the parties. Over the course of several years, as shown in the underlying litigation, the parties constantly revised and restructured their relationship, often orally without documentation. Yujuico Decl. ¶ 7. Indeed, when the economic crisis hit the Philippines, the parties did yet another restructure that resulted in the Amendment. Paragraph 20 of the Agreement, pursuant to which First Pacific agreed "to execute all instruments and take all such actions are reasonably requested and appropriate to effectuate this Agreement."[3]

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[3] It is well settled that a lender's acceptance of performance that deviates from the strict contact terms and overall cooperation and informality lulls borrowers into a sense of security, which cannot then be snatched away at a moments' notice. In *Lupertino v. Carbahal* 35 Cal. App. 3d 742 (1973), after undertaking a course of conduct that instilled in the borrowers a sense of comfort and reliance, the lender was thereafter

What is more, an arbitrator has the power and authority to require that First Pacific accept the tender of performance made this September. As recognized by the California Supreme Court in *Advanced Micro Devices v. Intel Corp.* (1994) 9 Cal. 4th 362, 374, this case, it "may require finding a way of approximating the impact of a breach that cannot with any certainty be reduced to monetary terms. **Passage of time and changed circumstances may have rendered any remedies suggested by the contract insufficient or excessive.**" *Id.* Indeed, the arbitrator in this case will be required to "bring his informed judgment to bear to reach a fair solution." *Steelworkers v. Enterprise Corp.* (1960) 363 U.S. 593, 597; 4 L.Ed.2d 1424, 1428; 80 S.Ct. 1358 (recognizing the need for flexibility in meeting a wide variety of situations, where draftsmen may never have thought of particular contingency).

The arbitrator's ability to fashion creatively an appropriate remedy based upon the parties' varying interpretations of the Agreement is consistent with the exceedingly broad powers that arbitrators generally enjoy and frequently implement. In *Moncharsh v. Heily Blasé* 3 Cal. 4th 1, 28 (1992); for example, the arbitrator resolved

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estopped from summarily abandoning such conduct without, at the very least, providing notice sufficient to allow the borrower to complete performance. Similarly, in *Lopez v. Bell* (1962) 207 Cal.App.2d 394, 399, the lender established a pattern of accepting late payments, thereby "lulling" the borrower into a sense of security. Ultimately, the court set aside the trustee's sale, holding that absent a specific notice reinstating the lender's intention to seek strict compliance with the terms of the contract, the lender's conduct amounted to a waiver of strict compliance and the right to forfeit the borrowers' interest. Id. at 397-98.

issues that the parties had not even agreed to arbitrate. Recognizing that resolution of "all contested issues" is exactly what the parties bargained for in the arbitration agreement, the court found that the arbitrator had not exceeded his authority and confirmed the award. *Id.* Similarly, in *Morris v. Zuckerman* 69 Cal. 2d 686, 688-94 (1968), the court confirmed an award which created a condition to the required sale, even though the original contract had no such limitation. *See also Anderman/Smith Co. v. Tenn Gas Pipeline Co.*, 98 F.2d 1215, 1217-20 (court approved award altering contract provisions for price changes in natural gas pricing).

2. The Stipulated Judgment And Arbitration Award are Unenforceable Forfeitures

An important principle that will guide the disposition of the arbitration is that "the law abhors a forfeiture." This principle is codified in Cal. Civil Code § 3275, which provides that "whenever, by the terms of an obligation, a party thereto incurs a forfeiture, or a loss in the nature of a forfeiture, by reason of his failure to comply with its provisions, he may be relieved therefrom, upon making full compensation to the other party, except in case of a grossly negligent, willful or fraudulent breach of duty." *Id. See also Nasir v. Sacramento County Office of the District Attorney* 11 Cal. App. 4th 976, 993-94 (1992).

The Agreement in this case contains two separate but equally abhorrent forfeitures. Indeed, Section 3275 has been interpreted to prohibit both the forfeiture of real property, where the borrower has in good faith attempted to avoid a default, and the forfeiture of money that

results from the enforcement of "hammer clauses" such as the $7.5 million stipulated Arbitration Award in this case. *Barkis v. Scott*, 34 Cal.2d. 116; *Scarbery v. Patch*, 184 Cal.App.2d 87 (1960); *Chambreau v. Coughlan*, 263 Cal.App.2d 712 (1968); *L.A. City Sch. Dist. v. Landier, Inc.*, 177 Cal.App.2d 744 (1960).

As to the first type of forfeiture, *Scarbery* is instructive. In *Scarbery*, the parties entered into a complicated lease option agreement, pursuant to which the plaintiff was to make payments for a specified period and that, upon an uncured default thereunder, the defendant would retain all amounts paid as liquidated damages and become the owner in fee of the property. For two years, the plaintiff made all payments and significantly improved the property. However, because of an intervening fire in the area and the plaintiff's unrelated physical illness, the property did not generate sufficient income for the plaintiff to meet his obligations under the lease option. Although the plaintiff subsequently tendered performance sufficient to reinstate the contract, the defendant refused and attempted to foreclose on the property.

In balancing the equities, the court found that because the plaintiff had paid $150,000 of a $200,000 obligation, his part performance was substantial enough to outweigh the degree of default, particularly since the court could easily measure the damage suffered by the default. The court also weighed heavily the fact that the plaintiff's nonpayment was due to inability rather than

unwillingness.[4] Accordingly, the Court ordered, pursuant to Section 3275, relief from the forfeiture.

Here, Claimants, like the defendant in *Scarbery*, face possible forfeiture of real property notwithstanding their good faith efforts to perform and the unforeseeable events in Asia. Further, Claimants have demonstrated an ongoing willingness to perform in full by, among other things, offering to repay the remaining sums on **better** terms than original terms and offering to place disputed amounts in escrow pending resolution of these issues. Under *Scarbery*, therefore, BVY is entitled to relief from the real property forfeiture now threatened by Plaintiff.

Section 3275 also applies in this instance to prevent enforcement of First Pacific's $2,300,000 "hammer clause." In *Chambreau, supra*, the parties stipulated to judgment for $8,025, but agreed to stay execution provided defendant paid for the lesser sum of $5,500.00 in regular monthly installments. Like First Pacific, the *Chambreau* plaintiff attempted to execute on the greater judgment based upon one late payment. The court properly disallowed the plaintiff's attempt to execute on the greater judgment, concluding that the defendant was entitled to equitable relief from forfeiture under Section 3275. Similarly, in *L.A. City Sch., supra*, the parties stipulated that the defendant would pay a sum certain in 8 annual installments, but that, following an uncured 30 day default, judgment could be entered for twice the unpaid balance. Although the defendant's request for

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[4] See also, *Ebbert v. Merchantile Trust Co. of Cal.* 213 Cal. 496, 500 (1931).

declaratory relief was found untimely, the court noted that the economic sanction constituted an improper penalty. *Id.* at 754.

Accordingly, First Pacific's proposed Judgment is unenforceable both as a real property forfeiture and a monetary penalty.

## IV. CONCLUSION

Based upon the foregoing, BVY respectfully submits that the Application must be denied.

Dated: October 9, 1998

Respectfully submitted,

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## APPENDIX III

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SUPERIOR COURT FOR THE STATE OF CALIFORNIA
IN AND FOR THE COUNTY OF SAN MATEO

| | |
|---|---|
| FIRST PACIFIC BANK LIMITED, a Honk Kong banking corporation,<br><br>Plaintiff,<br><br>vs.<br><br>THE BVY GROUP, a California corporation; et al.,<br><br>Defendants.<br><br>AND RELATED CROSS-ACTIONS | Case No. 391951<br><br>**MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF MOTION TO VACATE JUDGMENT**<br><br>**[C.C.P. § 473]**<br><br>**Date: December 3, 1998**<br><br>**Time: 9:00 a.m.**<br><br>**Dept: Law & Motion**<br><br>**(Filed Nov. 18, 1998)** |

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**APPENDIX IV**

Case No. AO85195

IN THE COURT OF APPEAL OF THE
STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION FOUR

| | |
|---|---|
| FIRST PACIFIC BANK LIMITED, a Hong Kong Banking Corporation, | ) |
| Plaintiff and Respondent, | ) |
| v. | ) |
| BENEDICTO YUJUICO, TERESITA YUJUICO, and THE BVY GROUP, INC., | ) |
| Defendants and Appellants. | ) |

Appeal from the Superior Court of San Mateo County
Case No. 391951
Honorable Judith Whitmer Kozloski, Judge

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**APPELLANTS' OPENING BRIEF**

---

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**APPENDIX V**

Case No. _____

IN THE
SUPREME COURT OF THE STATE OF CALIFORNIA

| | |
|---|---|
| FIRST PACIFIC BANK LIMITED, a Hong Kong Banking Corporation, | ) |
| Plaintiff and Respondent, | ) |
| v. | ) |
| BENEDICTO V. YUJUICO, TERESITA M. YUJUICO, and THE BVY GROUP, INC., | ) |
| Defendants, Appellants and Petitioners. | ) |

After a Decision by the Court of Appeal, First Appellate District, Division Four
Case No. A091568

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**PETITION FOR REVIEW AND REQUEST FOR IMMEDIATE STAY**

---

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**APPENDIX VI**

Case No. _____
[Related Case No. S089988]

IN THE

SUPREME COURT OF THE STATE OF CALIFORNIA

FIRST PACIFIC BANK LIMITED, a Hong Kong Banking Corporation,

Plaintiff and Respondent,

v.

BENEDICTO V. YUJUICO, TERESITA M. YUJUICO, and THE BVY GROUP, INC.,

Defendants, Appellants and Petitioners.

After a Decision by the Court of Appeal,
First Appellate District, Division Four
Case No. A085195

---

**PETITION FOR REVIEW**

---

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